ACCEPTANCES

INCLUDING

REGULATIONS AND RULINGS OF THE FEDERAL RESERVE BOARD;

INDEXED

The National City Company
National City Bank Building
New York

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THE NATIONAL CITY COMPANY
NATIONAL CITY BANK BUILDING
NEW YORK

APRIL, 1919

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REGULATIONS

Acceptances

BOTH trade and finance are peculiarly indebted to the acceptance, used by other financial centers for hundreds of years, but only recently permitted by our banking laws.

It is an emphatic contribution alike to the banker, the domestic merchant, the manufacturer, the importer, the exporter, and the investor.

As much as any other recent development, the acceptance has served to remove obstacles that stood in the way of a free cultivation of foreign markets, and in this connection it must be realized that a broad discount market is essential if we are successfully to compete for a share of the world's business.

It is the aim of this booklet to set forth simply and clearly just what an acceptance is, the technique of using it, and when and why it is an advantage to employ it.

Bank Acceptances

Under the authority granted by the Federal Reserve Act, any national bank may have outstanding acceptances aggregating 50 per cent of its capital and surplus. A bank may apply to the Federal Reserve Board, and receive permission to have outstanding acceptances up to 100 per cent of its capital and surplus, but in no event may acceptances against domestic transactions exceed 50 per cent of the capital and surplus of the bank. No acceptance may have a maturity later than six months after it is accepted. The amount accepted for any one person, firm or corporation must not exceed 10 per cent of the bank's capital and surplus. This 10 per cent limitation, however, does not apply where the bank is secured by some actual security growing out of the same transaction as the acceptance; the security must remain with the bank all the time the acceptance is outstanding.

In addition to the foregoing, after receiving authority from the Federal Reserve Board, a member bank may also accept up to 50 per cent of its capital and surplus, drafts drawn upon it for the purpose of furnishing dollar exchange. Drafts accepted for this purpose must mature within three months.

Many of the States have enacted legislation permitting the banks operating under their laws to make acceptances. The amount and restrictions vary with the different States. National Banks may accept drafts which

(1) Arise out of a transaction involving the importation or exportation of goods.

(2) Arise out of a transaction involving the domestic shipment of goods.

(3) Are secured by readily marketable goods in storage; or

(4) Are drawn for the purpose of furnishing dollar exchange.

The following examples, which are by way of illustration only, show how acceptances may be used under the various classifications.

Acceptances Arising Out of a Transaction Involving the Importation or Exportation of Goods

An Importation Acceptance

An importer desires to purchase some raw silk in Japan. He goes to his bank and explains the transaction. His credit standing being satisfactory, his bank issues, at his request, a Commercial Credit. This Credit authorizes the Japanese exporter to draw on the bank for the value of the silk which the importer is purchasing. The Credit limits the total amount of drafts which may be drawn under it, states that they must be drawn and negotiated on or before a certain date, and gives the usance; that is, that the drafts must mature thirty, sixty or ninety days, or whatever the period may be, after sight. It also stipulates what documents (shipping, insurance, etc.) must be attached to the drafts.

Since the importer wants to get his silk, there is not, ordinarily, time to wait until the Credit has reached the exporter through the mails. Usually, therefore, the information is cabled through a bank located in the vicinity of the exporter.

Upon receipt of this advice the exporter prepares his raw silk for shipment. As soon as he is in possession of the ocean bill of lading and other necessary documents he draws a draft on the bank in this country issuing the Credit for the value of the silk, the draft having a maturity in accordance with the terms of the Credit—let us say ninety days after sight. To the draft he attaches the documents referred to. He then takes the draft to his local bank, which purchases the draft at the current rate of exchange for ninety-day-sight dollar bills.

The shipping and other documents are all made out or indorsed so as to give the bank purchasing the draft title to the goods.

The bank in Japan now forwards the draft and documents to its agency or correspondent in this country. The papers are all presented to the bank issuing the Credit. If it finds everything in order, it accepts the draft, returning it to the party presenting it. The shipping and other documents are retained to be surrendered to the importer, probably in exchange for a trust receipt, to enable him to get his raw silk. The importer thus has ninety days in which to secure the raw silk and dispose of it before he is required to place his bank in funds to meet the maturing draft. The representative of the Japanese bank sells the acceptance in the open market at the prevailing rate for ninety-day bills.

For making this transaction possible the importer's bank charges him a small commission for accepting the draft. Only Credits issued by the well-known banks, of course, will be acceptable to the exporter, as he wants a bill which will command the best rate. This business is, therefore, usually handled by banks in the larger centers. The lesser-known institution usually has Credits required by its importers, issued by one of its large correspondents, under the guarantee of the smaller bank.

An Exportation Acceptance

An exporter here is negotiating for the sale of shoes to a firm in Argentina. He is not willing to ship the shoes and draw a draft direct on his customer, nor is he willing to sell him on open account. It is therefore necessary for the purchaser to finance the transaction by means of a banker's Credit. The purchaser goes to his bank in the Argentine and asks it to arrange a Credit with its correspondent in the United States to cover the value of the shoes. The Argentine banker, knowing that the purchaser is a satisfactory credit risk, requests his correspondent in this country to issue the Credit. The Argentine banker guarantees that the bank issuing the Credit will be placed in funds before the maturity of any drafts drawn on it under the Credit. The bank here then advises the exporter that, as requested by the purchaser, it will accept his drafts drawn on it up to a certain amount when the drafts are accompanied by the documents mentioned in the Letter of Credit.

These documents, of course, must represent the shoes which have been shipped. The Credit also probably states that it expires on a certain future date, thus making it necessary for the exporter to complete his end of the transaction within a reasonable time.

As soon as the exporter secures his necessary shipping and other documents he draws a draft on the bank here issuing the Credit, having a maturity in accordance with its terms, for the value of the shoes. The exporter presents the draft and documents to the bank issuing the Credit. Everything being as stipulated in the Credit, the bank accepts the draft and returns it to the exporter, who sells it in the market and thus receives payment for his shoes. The documents are forwarded to the bank requesting that the Credit be opened, and are probably released by them to the purchaser. The Argentine bank, through remittances, or by charge against its balance in this country, places its correspondent in funds to meet the draft at maturity.

Acceptances Arising Out of Transactions Involving the Domestic Shipment of Goods

A manufacturer, desiring to finance his purchases of raw material through the medium of bankers' acceptances, requests his bank to issue a Credit in favor of the people from whom he is purchasing. The Credit should be for an amount not exceeding, of course, the value of the goods being purchased. The drafts might have a usance which would give the purchaser time to make up the raw material and sell the manufactured product. This maturity should not, however, exceed ninety days, as bills with a longer maturity do not have as ready marketability. This arrangement being satisfactory to the seller, he will ship his goods, draw a draft for their value on the bank issuing the Credit, and forward the draft and shipping documents to the bank. It must be borne in mind that the shipping documents must be so issued or indorsed as to give the bank title to the goods. The bank accepts the draft and returns it to the shipper, who disposes of it at the prevailing discount rate. The documents are turned over to the

manufacturer, probably under a trust receipt, and he is enabled to secure his raw material, manufacture and sell his goods. Before maturity he is required to place the bank in funds to meet the draft.

Acceptances Which Are Secured by Readily Marketable Goods in Warehouse

A clothing manufacturer, for example, desires to carry his stock of wool through the use of bankers' acceptances. He places the wool in a warehouse, draws a draft on his bank for the value of the wool, attaching the warehouse receipts as collateral. The draft, after acceptance, is returned to him to be sold, the warehouse receipts being retained by the bank. The wool must be stored in a warehouse which is independent of the manufacturer; that is, the manufacturer must not have any control of the wool as long as the warehouse receipts are outstanding. It is, of course, possible to secure possession of the original warehouse receipts by substituting other warehouse receipts for wool, but if the manufacturer desires to take down wool without substitution he should give the bank the cash value of the wool taken, for the bank should be secured either by warehouse receipts or cash all the time its acceptance is out.

Drafts Drawn for the Purpose of Furnishing Dollar Exchange

It sometimes happens that persons in foreign countries having obligations to meet here are not able to secure dollar exchange to remit in settlement. To provide for any such contingency the law and the regulations of the Federal Reserve Board permit banks here to accept drafts drawn on them by banks in certain foreign countries for the purpose of furnishing such dollar exchange. A bank desiring to accept bills drawn for this purpose must first make application to the Federal Reserve Board for permission to do so. The restrictions surrounding acceptances for this purpose are fully set forth in the regulations and informal rulings of the Board.

As An Investment

Prime bank acceptances are especially desirable as an investment because they combine in a degree not found in any other commercial instrument the three important factors of safety, short maturity, and ready convertibility into cash.

Safety

When a bank accepts a draft it has created an obligation which it must, if it is to retain its standing, pay at maturity. The acceptance of a bank is as good as the bank itself, ranking with its cashier's check or certificate of deposit. But the drawer and indorsers of an acceptance are also liable, providing it is not paid at maturity and is properly protested. If one is satisfied that the funds he has deposited in his bank are safe, he can certainly find no objection from the

standpoint of security to purchasing the acceptance of that same bank, or of another bank equally as good or better.

England, which heretofore has financed the foreign commerce of the world, has been enabled to do so largely because her bankers have purchased large amounts of acceptances and have loaned enormous sums at very low rates to dealers to enable them to carry bills. Their long experience has shown them that prime acceptances are the safest short-term investment they can find.

Our prime acceptances are just as good as those which have proved so satisfactory in England, and possibly better, because an eligible acceptance here is against a shipment of goods or is secured by goods; the only exception being bills for dollar exchange, in which case they are drawn by a bank and accepted by a bank.

Maturity

Few acceptances appear in this market having a maturity longer than four months. The great majority are drawn payable ninety days after sight. Within these limitations the investor can usually secure in the market bills approximating any maturity he may desire, whether it be for only three or four weeks or for the longer period. We have no other form of investment which can compete with acceptances in this respect.

The two features just mentioned make prime acceptances especially fitted as an investment for funds of corporations, firms or individuals, being accumulated for a special purpose, which will be paid out within a short time, such as funds for the payment of a dividend.

Convertibility Into Cash

Under the provisions of the Federal Reserve Act, the various Federal Reserve Banks may purchase acceptances in the open market. The acceptances must, of course, be eligible; that is, must arise out of one of the four kinds of transactions mentioned heretofore.

As will be seen, the acceptance of any National Bank is eligible. Non-member banks and bankers may make their acceptances eligible by filing with the Federal Reserve Bank a statement of financial condition, in form to be approved by the Federal Reserve Board. They must also agree in writing with the Federal Reserve Bank to inform it, upon request, concerning the transactions underlying their acceptances. Acceptances which the Reserve Banks cannot purchase or rediscount are termed ineligible, and do not command as favorable a rate in the market as eligible bills.

The figures in any number of the Federal Reserve Bulletin will show the large volume of acceptances which have been purchased by the various Federal Reserve Banks. This power to purchase and willingness on the part of the Federal Reserve Banks to do so, as evidenced by the extent of their transactions, make a prime eligible acceptance in the hands of a member bank the most liquid investment that bank has. A member bank desiring to dispose of the acceptances of other banks which it holds, indorses those acceptances and sells them to its Federal Reserve Bank at the prevailing rate for the purchase of acceptances. It should be noted that bank acceptances are sold to the Federal

Reserve Banks, not rediscounted. The purchase rates for prime indorsed bills are usually below the rediscount rates for paper. The nearer the acceptance approaches maturity the more favorable rate it commands at the Reserve Banks.

The non-member bank, corporation or individual desiring to dispose of acceptances before maturity has always been able to do so to dealers in the open market, and ordinarily at very little difference from the rate at which the bills were purchased. In this connection it must be remembered that acceptances are discounted for the number of days they have to run from date of sale until maturity.

Bank acceptances are often drawn for odd amounts, representing the value of a shipment. They vary in size from a few hundred dollars to several hundred thousand dollars. It is, therefore, usually possible for an investor to purchase approximately any amount he may desire.

To banks and others desiring to invest a portion of their funds in an obligation of this character, The National City Company offers at all times a carefully selected list of prime bank acceptances. A copy of this list will be forwarded on request.

Trade Acceptances

A Trade Acceptance is a draft drawn by the seller of goods on the purchaser and accepted by him. It must bear a statement on its face to the effect that it represents a purchase of goods by the acceptor from the drawer of the draft.

If the acceptance is not paid at maturity, and is properly protested, recourse may be had by the holder to any indorser and to the drawer.

Being drawn against actual current transactions, and being paper bearing at least two names, the Federal Reserve Banks make preferential rates for the rediscount of trade acceptances as compared with single-name paper. They may also purchase trade acceptances in the open market.

The National City Company also offers to banks and investors prime domestic trade acceptances, as well as trade acceptances drawn in a foreign country, accepted by firms in this country, and bearing a bank indorsement.

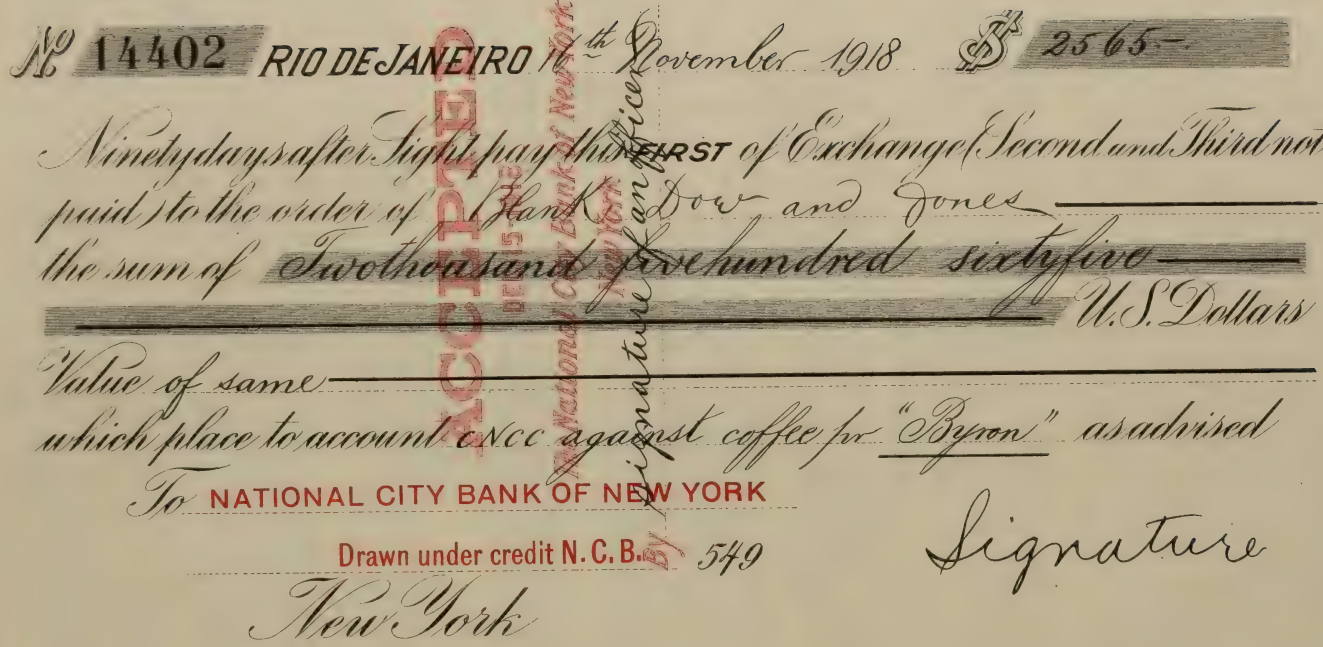
ILLUSTRATIONS

The specimen bills shown in the accompanying illustrations are from forms actually used.

It is not necessary that the bill follow exactly the language of these forms.

On the bill drawn in a foreign country the nature of the merchandise and very often the steamer name and the markings are included in the description of the articles against which the bill is drawn; the only purpose of this is to make it easy for the accepting bank to place the draft against the proper credit. The name of the firm, "Blank, Doe & Jones," usually represents the original purchaser or discounter of the bill. This purchaser is almost invariably either a bank or a discounting house.

On the bill drawn locally the maker signs the bill and draws it under a credit which John Doe and John Smith Co. have arranged with the bank. The maker has this accepted and either sells or discounts it and thereby receives payment for the "Dye Stuffs" sold to John Doe and John Smith Co. At maturity the bank will look to John Doe and John Smith Co. direct or, if the credit is a guaranteed one, to the guarantors for settlement.


No 14402 RIO DE JANEIRO 16th November 1918 $ 2565-

Ninety days after Sight pay this FIRST of Exchange (Second and Third not paid) to the order of Messrs Dow and Jones

the sum of Two thousand five hundred sixty five U.S. Dollars

Value of same

which place to account of N.C.C. against coffee per "Byron" as advised

To NATIONAL CITY BANK OF NEW YORK

Drawn under credit N.C.B. By 549

New York

Signature

ACCEPTED DEC 5 1918 National City Bank of New York

Signature and Indorsement

SPECIMEN BILL DRAWN IN FOREIGN COUNTRY

((Exchange for $ 9.100 00/100 New York JAN 8 - 1919

Ninety ——— days after sight of this First

of Exchange (~~Second unpaid~~) pay to the order of

Ourselves ———

Nine thousand One hundred 00/100 Dollars.

"Value received against mdse per S/S Empress of Japan"

A/c of John Doe and John Smith Co. Worcester, Mass.

Drawn under Credit National City Bank of New York No. 6408. Nov 22/15

Sye Stuffs.

ACCEPTED JAN. 1919 The National City Bank of New York

By Signature of Officer

To NATIONAL CITY BANK OF NEW YORK

NEW YORK CITY

No. D8116

Signature

SPECIMEN BILL DRAWN LOCALLY

Regulations on Acceptances

REDISCOUNTS UNDER SECTION 13

Regulation A, Series of 1917 *June* 22, 1917

A—NOTES, DRAFTS, AND BILLS OF EXCHANGE

I. General Statutory Provisions

(1) Any Federal Reserve Bank may discount for any of its member banks any note, draft, or bill of exchange, provided—

(2) (a) It has a maturity at the time of discount of not more than 90 days, exclusive of days of grace; but if drawn or issued for agricultural purposes, or based on live stock, it may have a maturity at the time of discount of not more than six months, exclusive of days of grace.

(3) (b) It arose out of actual commercial transactions; that is, it must be a note, draft, or bill of exchange which has been issued or drawn for agricultural, industrial, or commercial purposes, or the proceeds of which have been used or are to be used for such purposes.

(4) (c) It was not issued for carrying or trading in stocks, bonds, or other investment securities, except bonds and notes of the Government of the United States.

(5) (d) The aggregate of notes, drafts and bills bearing the signature or indorsement of any one borrower, whether a person, company, firm, or corporation, rediscounted for any one member bank shall at no time exceed 10 per cent of the unimpaired capital and surplus of such bank; but this restriction shall not apply to the discount of bills of exchange drawn in good faith against actually existing values.

(6) (e) It is indorsed by a member bank.

(7) (f) It conforms to all applicable provisions of this regulation.

II. General Character of Notes, Drafts, and Bills of Exchange Eligible

(8) The Federal Reserve Board, exercising its statutory right to define the character of a note, draft, or bill of exchange eligible for rediscount at a Federal Reserve Bank, has determined that—

(9) (a) It must be a note, draft, or bill of exchange the proceeds of which have been used or are to be used in producing, purchasing, carrying, or marketing goods[1] in one or more of the steps of the process of production, manufacture, or distribution.

(10) (b) It must not be a note, draft, or bill of exchange the proceeds of which have been used or are to be used for permanent or fixed investments of any kind, such as land, buildings, or machinery.

(11) (c) It must not be a note, draft, or bill of exchange the proceeds of which have been used or are to be used for investments of a purely speculative character.

[1] *When used in this regulation the word "goods" shall be construed to include goods, wares, merchandise, or agricultural products, including live stock.*

(12) (d) It may be secured by the pledge of goods or collateral, provided it is otherwise eligible.

III. Applications for Rediscount

(13) All applications for the rediscount of notes, drafts, or bills of exchange must contain a certificate of the member bank, in form to be prescribed by the Federal Reserve Bank, that to the best of its knowledge and belief such notes, drafts, or bills of exchange have been issued for one or more of the purposes mentioned in *II* (a) (*see par.* 9).

IV. Promissory Notes

(14) (*a*) *Definition.* A promissory note, within the meaning of this regulation, is defined as an unconditional promise, in writing, signed by the maker, to pay in the United States, at a fixed or determinable future time, a sum certain in dollars to order or to bearer.

(15) (*b*) *Evidence of eligibility and requirement of statements.* A Federal Reserve Bank must be satisfied by reference to the note, or otherwise, that it is eligible for rediscount. Compliance of a note with *II* (b) (*see par.* 10) may be evidenced by a statement of the borrower showing a reasonable excess of quick assets over current liabilities. The member bank shall certify in its application whether the note offered for rediscount has been discounted for a depositor or another member bank, or whether it has been purchased from a non-depositor. It must also certify whether a financial statement of the borrower is on file.

(16) Such financial statements must be on file with respect to all notes offered for rediscount which have been purchased from sources other than a depositor or a member bank. With respect to any other note offered for rediscount, if no statement is on file, a Federal Reserve Bank shall use its discretion in taking the steps necessary to satisfy itself as to eligibility. It is authorized to waive the requirement of a statement with respect to any note discounted by a member bank for a depositor or another member bank—

(17) (1) If it is secured by a warehouse, terminal, or other similar receipt covering goods in storage;

(18) (2) If the aggregate of obligations of the borrower rediscounted and offered for rediscount at the Federal Reserve Bank is less than a sum equal to 10 per cent of the paid-in capital of the member bank and does not exceed $5,000.

V. Drafts, Bills of Exchange, and Trade Acceptances

(19) (*a*) *Definition.* 1. *Draft or bill of exchange.* 2. *Trade acceptance.* A draft or bill of exchange, within the meaning of this regulation, is defined as an unconditional order in writing, addressed by one person to another, other than a banker, as defined under B (b) (*see par.* 27), signed by the person giving it, requiring the person to whom it is addressed to pay in the United States, at a fixed or determinable future time, a sum certain

in dollars to the order of a specified person; and a trade acceptance is defined as a draft or bill of exchange drawn by the seller on the purchaser of goods sold and accepted by such purchaser.

(20) (*b*) *Evidence of eligibility.* A Federal Reserve Bank shall take such steps as it deems necessary to satisfy itself as to the eligibility of the draft or bill offered for rediscount, unless it presents prima facie evidence thereof or bears a stamp or certificate affixed by the acceptor or drawer showing that it is a trade acceptance.

VI. Six Months' Agricultural Paper

(21) (*a*) *Definition.* Six months' agricultural paper, within the meaning of this regulation, is defined as a note, draft, bill of exchange, or trade acceptance, drawn or issued for agricultural purposes, or based on live stock; that is, a note, draft, bill of exchange, or trade acceptance the proceeds of which have been used, or are to be used, for agricultural purposes, including the breeding, raising, fattening, or marketing of live stock, and which has a maturity at the time of discount of not more than six months, exclusive of days of grace.

(22) (*b*) *Eligibility.* To be eligible for rediscount, six months' agricultural paper, whether a note, draft, bill of exchange, or trade acceptance, must comply with the respective sections of this regulation which would apply to it if its maturity were 90 days or less.

VII. Commodity Paper

(23) (*a*) *Definition.* Commodity paper, within the meaning of this regulation, is defined as a note, draft, bill of exchange, or trade acceptance, accompanied and secured by shipping documents or by a warehouse, terminal, or other similar receipt covering approved and readily marketable, non-perishable staples properly insured.

(24) (*b*) *Eligibility.* To be eligible for rediscount at the special rates authorized to be established for commodity paper, such a note, draft, bill of exchange, or trade acceptance must also comply with the respective sections of this regulation applicable to it, must conform to the requirements of the Federal Reserve Bank relating to shipping documents, receipts, insurance, etc., and must be a note, draft, bill of exchange, or trade acceptance on which the rate of interest or discount—including commission—charged the maker, does not exceed 6 per cent per annum.

(25) (*c*) *Suspension of commodity rate.* As the special rate on commodity paper is intended to assist actual producers during crop-moving periods, and is not designed to benefit speculators, the Board reserves the right to suspend the special rates herein provided whenever it is apparent that the movement of crops, which this rate is intended to facilitate, has been practically completed.

B.—Bankers' Acceptances

(26) (*a*) *General statutory provisions.* 1. *For Discount:* (*a*) *Maturity.* (*b*) *Indorsement.* (*c*) *Transactions involved.* (*d*) *Security.* 2. *Acquire drafts or bills to furnish dollar exchange.*

Any Federal Reserve Bank may discount for any of its member banks bankers' acceptances which have a maturity at the time of discount of not more than three months' sight, exclusive of days of grace, which are indorsed by at least one member bank, and which grow out of transactions involving the importation or exportation of goods; or which grow out of transactions involving the domestic shipment of goods, provided shipping documents are attached at the time of acceptance; or which are secured at the time of acceptance by a warehouse receipt (*see par.* 98), or other such document, conveying or securing title covering readily marketable staples. Any Federal Reserve Bank may also acquire drafts or bills of exchange drawn on member banks by banks or bankers in foreign countries or dependencies or insular possessions of the United States for the purpose of furnishing dollar exchange.

(27) (*b*) *Definition.*

A banker's acceptance within the meaning of this regulation is defined as a draft or bill of exchange of which the acceptor is a bank or trust company, or a firm, person, company, or corporation engaged in the business of granting bankers' acceptance credits.

(28) (*c*) *Eligibility.* 1. *For rediscount:* (*a*) *Drawn under credit opened.* (*b*) *Security.* 2. *Acquire drafts or bills:* (*a*) *Drawn to furnish dollar exchange.* (*b*) *Accepted.* (*c*) *When acquired.*

To be eligible for rediscount, the bill must have been drawn under a credit opened for the purpose of conducting or settling accounts resulting from a transaction or transactions involving (1) the shipment of goods between the United States and any foreign country, or between the United States and any of its dependencies or insular possessions, or between foreign countries; or (2) the domestic shipment of goods, provided shipping documents are attached at the time of acceptance; or it must be a bill which is secured at the time of acceptance by a warehouse receipt or other such document, conveying or securing title covering readily marketable staples. Any Federal Reserve Bank may also acquire drafts or bills drawn by a bank or banker in a foreign country or dependency or insular possession of the United States for the purpose of furnishing dollar exchange, and accepted by a member bank in accordance with the provisions of Regulation C (*see par.* 53). Such drafts or bills may be acquired prior to acceptance provided they have the indorsement of a member bank.

(29 (*d*) *Evidence of eligibility. Stamp or certificate.*

A Federal Reserve Bank must be satisfied, either by reference to the acceptance itself, or otherwise, that it is eligible for rediscount. Satisfactory evidence of eligibility may consist of a stamp or certificate affixed by the acceptor in form satisfactory to the Federal Reserve Bank.

Open-Market Purchases of Bills of Exchange, Trade Acceptances, and Bankers' Acceptances Under Section 14*

Regulation B, Series of 1917 — *June* 22, 1917

I. General Statutory Provisions

(30) *Paper eligible for rediscount with or without member bank indorsement.* Section 14 of the Federal Reserve Act permits Federal Reserve Banks, under rules and regulations to be prescribed by the Federal Reserve Board, to purchase and sell in the open market from banks, firms, corporations, or individuals, bankers' acceptances and bills of exchange of the kinds and maturities made eligible by the Act for rediscount, with or without the indorsement of a member bank.

II. General Character of Bills and Acceptances Eligible

(31) The Federal Reserve Board, exercising its statutory right to regulate the purchase of bills of exchange and acceptances, has determined that a bill of exchange or acceptance, to be eligible for purchase by Federal Reserve Banks under section 14—

(32) (*a*) *Investment securities.* Must not have been issued for carrying or trading in stocks, bonds, or other investment securities, except bonds and notes of the Government of the United States.

(33) (*b*) *Permanent or speculative investments.* Must not be a bill the proceeds of which have been used or are to be used for permanent or fixed investments of any kind, such as land, buildings, machinery, or for investments of a merely speculative character.

(34) (*c*) *Accepted by drawee unless secured.* Must have been accepted by the drawee prior to purchase by a Federal Reserve Bank unless it is accompanied and secured by shipping documents or by a warehouse, terminal, or other similar receipt conveying security title.

(35) (*d*) *Security.* May be secured by the pledge of goods[1] or collateral, provided it is otherwise eligible.

(36) In addition to the above general requirements, each bill of exchange and trade acceptance purchased under the terms of this regulation must also conform to the more specific requirements set forth under *III* (*see par.* 37-40), and each banker's acceptance must also conform to the more specific requirements set forth under *IV* (*see par.* 41-48).

III. Bills of Exchange and Trade Acceptances

(37) (*a*) *Definition.*
1. *Bill of exchange.*
2. *Trade acceptance.*

A bill of exchange, within the meaning of this regulation, is defined as an unconditional order in writing, addressed by one person to another, other than a banker, as defined under *IV* (a), (*see par.* 41), signed by the person giving it, requiring the person to

*See par. 164-178 for Informal Rulings and Opinions of Counsel.

[1] *When used in this regulation the word "goods" shall be construed to include goods, wares, merchandise, or agricultural products, including live stock.*

whom it is addressed to pay in the United States, at a fixed or determinable future time, a sum certain in dollars to the order of a specified person; and a trade acceptance is defined as a bill of exchange drawn by the seller on the purchaser of goods sold, and accepted by such purchaser.

(38) (*b*) *Eligibility. 1. Commercial transaction. 2. Maturity.* To be eligible for purchase the bill must have arisen out of an actual commercial transaction, domestic or foreign; that is, it must be a bill which has been issued or drawn for agricultural, industrial, or commercial purposes, or the proceeds of which have been used, or are to be used, for the purpose of producing, purchasing, carrying or marketing goods in one or more of the steps of the process of production, manufacture, or distribution. It must have a maturity at time of purchase of not more than ninety days, exclusive of days of grace.

(39) (*c*) *Evidence of eligibility. Stamp or certificate.* A Federal Reserve Bank shall take such steps as it deems necessary to satisfy itself as to the eligibility of the bill offered for purchase, unless it presents prima facie evidence thereof or bears a stamp or certificate affixed by the acceptor or drawer showing that it is a trade acceptance.

(40) (*d*) *Statements.* Unless indorsed by a member bank, a bill is not eligible for purchase until a satisfactory statement has been furnished of the financial condition of one or more of the parties thereto.

IV. Bankers' Acceptances

(41) (*a*) *Definition.* A bankers' acceptance, within the meaning of this regulation, is a bill of exchange of which the acceptor is a bank or trust company, or a firm, person, company, or corporation engaged in the business of granting bankers' acceptance credits.

(42) (*b*) *Eligibility. 1. Maturity. 2. Drawn under credit opened. 3. Or to furnish dollar exchange.* To be eligible for purchase, the bill—which must have a maturity at time of purchase of not more than three months, exclusive of days of grace—must have been drawn under a credit opened for the purpose of conducting or settling accounts resulting from a transaction or transactions involving—

(43) (1) The shipment of goods between the United States and any foreign country, or between the United States and any of its dependencies or insular possessions, or between foreign countries, or

(44) (2) The shipment of goods within the United States, provided the bill at the time of its acceptance is accompanied by shipping documents, or

(45) (3) The storage within the United States of readily marketable goods, provided the acceptor of the bill is secured by warehouse, terminal, or other similar receipt, or

(46) (4) The storage within the United States of goods which have been actually sold, provided the acceptor of the bill is secured by the pledge of such goods; or it must be a bill drawn by a bank or banker in a foreign country or dependency or insular possession of the United States for the purpose of furnishing dollar exchange. In this latter case the bank or banker drawing the bill must be in a country, dependency, or possession whose usages of trade have been determined by the Federal Reserve Board to require the drawing of bills of this character.

(47) (*c*) *Evidence of eligibility. Stamp or certificate.* A Federal Reserve Bank must be satisfied either by reference to the acceptance itself, or otherwise, that it is eligible for purchase. Satisfactory evidence of eligibility may consist of a stamp or certificate affixed by the acceptor, in form satisfactory to the Federal Reserve Bank. No evidence of eligibility is required with respect to a bill accepted by a national bank.

(48) (*d*) *Statements.* 1. *Financial statement; and* 2. *Information concerning transactions.* Bankers' acceptances, other than those accepted or indorsed by member banks, shall be eligible for purchase only after the acceptor has furnished a satisfactory statement of financial condition in form to be approved by the Federal Reserve Board, and has agreed in writing with a Federal Reserve Bank to inform it upon request concerning the transactions underlying such acceptances.

Acceptance by Member Banks of Drafts and Bills of Exchange

Regulation C, Series of 1917 *June* 22, 1917

A—Acceptance of Drafts or Bills of Exchange Drawn Against Domestic or Foreign Shipments of Goods or Secured by Warehouse Receipts Covering Readily Marketable Staples

I. Statutory Provisions

(49) (*a*) *Maturity.* (*b*) *Transactions involved.* (*c*) *Security.* (*d*) *Amount limited.* Under the provisions of the fifth paragraph of section 13 of the Federal Reserve Act, as amended by the acts of September 7, 1916, and June 21, 1917, any member bank may accept drafts or bills of exchange drawn upon it, having not more than six months' sight to run, exclusive of days of grace, which grow out of transactions involving the importation or exportation of goods; or which grow out of transactions involving the domestic shipment of goods, provided shipping documents conveying or securing title are attached at the time of acceptance; or which are secured at the time of acceptance by a warehouse receipt (*see par.* 98), or other such document conveying or securing title covering readily marketable staples. This paragraph limits the amount which any bank shall accept for any one person, company, firm, or corporation, whether in a foreign or domestic transaction, to

an amount not exceeding at any time, in the aggregate, more than 10 per centum of its paid-up and unimpaired capital stock and surplus (*see par.* 127-129). This limit, however, does not apply in any case where the accepting bank is secured either by attached documents or by some other actual security (*see par.* 119-120) growing out of the same transaction as the acceptance (*see par.* 130, 166-168). The law also provides that any bank may accept such bills up to an amount not exceeding at any time, in the aggregate, more than one-half of its paid-up and unimpaired capital stock and surplus; or, with the approval of the Federal Reserve Board, up to an amount not exceeding at any time, in the aggregate, more than 100 per centum of its paid-up and unimpaired capital stock and surplus. In no event, however, shall the aggregate amount of acceptances growing out of domestic transactions exceed 50 per centum of such capital stock and surplus.

II. Regulations

(50) 1. *Application to accept up to 100 per cent of capital and surplus.* Under the provisions of the law referred to above, the Federal Reserve Board has determined that any member bank having an unimpaired surplus equal to at least 20 per centum of its paid-up capital, which desires to accept drafts or bills of exchange drawn for the purposes described above, up to an amount not exceeding at any time, in the aggregate, 100 per centum of its paid-up and unimpaired capital stock and surplus, may file an application for that purpose with the Federal Reserve Board. Such application must be forwarded through the Federal Reserve Bank of the district in which the applying bank is located.

(51) 2. *Report.* The Federal Reserve Bank shall report to the Federal Reserve Board upon the standing of the applying bank, stating whether the business and banking conditions prevailing in its district warrant the granting of such application.

(52) 3. The approval of any such application may be rescinded upon 90 days' notice to the bank affected.

B—ACCEPTANCE OF DRAFTS OR BILLS OF EXCHANGE DRAWN FOR THE PURPOSE OF CREATING DOLLAR EXCHANGE

I. Statutory Provisions

(53) 1. *Maturity.* 2. *Drawn by.* 3. *To create dollar exchange.* Section 13 of the Federal Reserve Act also provides that any member bank may accept drafts or bills of exchange drawn upon it having not more than three months' sight to run, exclusive of days of grace, drawn, under regulations to be prescribed by the Federal Reserve Board, by banks or bankers in foreign countries, or dependencies or insular possessions of the United States for the purpose of furnishing dollar exchange as required by the usages of trade in the respective countries, dependencies, or insular possessions.

(54) *Amount limited.* No member bank shall accept such drafts or bills of exchange for any one bank to an amount exceeding in the aggregate 10 per centum of the paid-up and unimpaired capital and surplus of the accepting bank unless the draft or bill of exchange is accompanied by documents conveying or securing title or by some other adequate security. No member bank shall accept such drafts or bills in an amount exceeding at any time in the aggregate one-half of its paid-up and unimpaired capital and surplus. This 50 per cent limit is separate and distinct from and not included in the limits placed upon the acceptance of drafts and bills of exchange as described under section A of this regulation (*see par.* 49-52, 116).

II. Regulations

(55) *Application.* Any member bank desiring to accept drafts drawn by banks or bankers in foreign countries or dependencies or insular possessions of the United States for the purpose of furnishing dollar exchange, shall first make an application to the Federal Reserve Board setting forth the usages of trade in the respective countries, dependencies, or insular possessions in which such banks or bankers are located.

(56) *Approval and Notification.* If the Federal Reserve Board should determine that the usages of trade in such countries, dependencies, or possessions, require the granting of the acceptance facilities applied for, it will notify the applying bank of its approval and will also publish in the Federal Reserve Bulletin the name or names of those countries, dependencies, or possessions in which banks or bankers are authorized to draw on member banks whose applications have been approved for the purpose of furnishing dollar exchange.*

(57) *Modify or revoke approval.* The Federal Reserve Board reserves the right to modify, or on 90 days' notice to revoke, its approval, either as to any particular member bank or as to any foreign country or dependency or insular possession of the United States in which it has authorized banks or bankers to draw on member banks for the purpose of furnishing dollar exchange.

**In the September,* 1917, *Bulletin appeared the following: "Applications for power to accept drafts drawn by banks and bankers in South American countries have been received from several institutions, and the Board has voted to permit drafts drawn upon member banks by banks or bankers in any Central or South American country for the purposes specified in the Federal Reserve Act, to be accepted by such member banks, upon application to and approval by the Board."*

In the October, 1918, *Bulletin appeared the following: "Banks and bankers in the following countries have been authorized by the Federal Reserve Board to draw drafts for the purpose of furnishing dollar exchange: Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, Nicaragua, Peru, Porto Rico, Santo Domingo, Uruguay, Venezuela, and Trinidad."*

Informal Rulings of the Federal Reserve Board and Opinions of Counsel

Trade Acceptances

December 24, 1917

(58) The Federal Reserve Board has ruled on several occasions that a bill of exchange drawn by the seller of goods and accepted by the purchaser of those goods is a trade acceptance, regardless of whether or not the purchaser intends to resell the goods or to use them for his own purpose, and that, therefore, a retail dealer may finance the sale of his goods to a retail customer by means of the trade acceptance.

The Board believes, therefore, that a bill drawn by a retail dealer on his retail customer to finance the sale of goods to that customer is a trade acceptance within the meaning of the Board's regulations, even though it is drawn after the purchaser has failed to remit promptly on an open account.

The Board is also of the opinion, however, that to attempt to use the trade acceptance in this manner as a means of liquidating an otherwise slow account would involve considerable danger to the primary purposes of the trade-acceptance movement, and would subordinate the trade acceptance to the open account by suggesting it as a last resort for bad debts. While, therefore, trade acceptances of this character should probably be considered eligible as a matter of law, nevertheless member banks and Federal Reserve Banks should be encouraged to discriminate against them as far as possible for the reason just stated.

Form of Trade Acceptance

(*To an Individual*) *June* 25, 1918

(59) Receipt is acknowledged of your letter outlining two forms of trade acceptances and requesting an expression of the Board's preference. The matter was referred to counsel, and the Board concurs with his opinion that Form 2 would seem to be the most desirable, since it contains a specific request to pay the draft, instead of a mere implied request or waiver of further notice.

(*From an Individual*) *June* 5, 1918

(60) Various clients of ours send their trade acceptances to all States of the Union and wish to have them so worded that it would be proper for a bank in any State, including the State where the negotiable-instrument law has not been enacted or it has been modified, to pay the acceptance without previously notifying the acceptor.

Will you advise me if the wording in either form of indorsement, as noted below, should be sufficient warrant for the bank to pay the acceptance from funds of the acceptor in their hands without notification to the acceptor?

(*Form* 1)

Accepted at.....191..
Bank where payable.....
(Without further notice to acceptor.)
Address of bank.....
(If no bank, address of acceptor.)

Name .....
(Acceptor's authorized signature.)
By .....

(*Form* 2)

Accepted at.....191..
Bank where payable.....
(If no bank, address of acceptor.)
Address .....
(Pay as specified, charge to the account of)
Name .....
(Acceptor's authorized signature.)
By .....

Conditions Attached to and Affecting Negotiability of Bills of Exchange and Acceptances

(*Opinion of Counsel*) *February* 2, 1915

(61) A bill of exchange, in order to be negotiable, must be an unconditional order to pay, on demand or at a fixed or determinable future time, a certain sum of money to order or to bearer. If payment is dependent upon the happening of a certain contingency the bill is conditional and non-negotiable. If payment is confined to the proceeds of a particular fund and is not chargeable to the general credit of the drawer the bill is conditional and non-negotiable.

A general acceptance of a conditional bill or a conditional acceptance of an unconditional bill makes the acceptance a conditional one and destroys its negotiability.

There is some doubt in the courts whether the mere reference to a particular consignment of goods makes the bill conditional, some courts stating that it is merely an indication of the fund out of which the drawee is to reimburse himself; other courts holding that it makes the bill conditional because limiting payment to the proceeds of the particular shipment referred to. There is no doubt, however, that a reference, in general terms, on the face of an accepted bill to the fact that it is based on the exportation or importation of goods, would not make it conditional and non-negotiable, and it would not, therefore, be ineligible for discount under the provisions of section 13 of the Federal Reserve Act.

Form of Draft

(*To a National Bank*) *January* 17, 1918

(62) You ask whether there is any objection to the form of draft used by some of your cotton mills which are purchasing cotton from merchants, and whether such a draft made payable at sight and accepted by the drawee is negotiable if it contains the following provision: "With interest at the rate of 6 per cent. per annum if payment is delayed."

In reply you are advised:

(a) That the Board knows of no objection to the use of the draft in the form submitted.

(b) If made payable at sight and accepted by the drawee it should not be discounted as a draft or bill of exchange, since in practically all States a draft payable at sight becomes payable without grace as soon as presented or exhibited to the drawee. This being true, if the holder presented it for acceptance instead of for payment the drawer and indorsers would probably be released and the holder would have recourse only against the acceptor as the party primarily liable. Such a draft would not be eligible for rediscount with a Federal Reserve Bank, since it would not have a fixed maturity of less than 90 days.

To all intents and purposes it would be the promissory note of the acceptor and his liability to the bank would be subject to the limitations of section 5200 Revised Statutes.

(c) In the opinion of the Board the insertion of the language suggested would not affect the negotiability of the instrument if it is construed to mean that interest at the rate of 6 per cent. per annum is to begin to run from date of maturity. It is inadvisable, however, in any case to insert language the meaning of which is ambiguous, and the clause suggested in your letter is open to this criticism.

Drafts Payable With Interest

(*Opinion of Counsel*) *February* 19, 1917

(63) A provision in a draft or bill of exchange that it is payable "with interest at the rate of — per cent. per annum after maturity if payment is delayed" does not affect the negotiability of the instrument.

Draft Drawn for Insurance Premium as a Trade Acceptance

(*To a Federal Reserve Bank*) *March* 6, 1918

(64) A draft drawn by a casualty company against a policyholder for premiums could hardly be said to be a draft by the seller on the purchaser of goods sold and would not, in the opinion of the Board, come within the Board's present definition of a trade acceptance.

It is, of course, within the power of the Board to extend this definition so as to include drafts drawn for insurance, services rendered, etc., if it determines this to be advisable. It would, however, require rather a forced construction to treat a draft drawn for an insurance premium as a trade acceptance under the present definition of the Board.

Drafts for Purchase of Electrical Goods, Including Cost of Installation, as Trade Acceptance

(*To a Federal Reserve Bank*) *February* 23, 1918

(65) May drafts drawn for the purchase price of electrical and mechanical goods, which include the cost of installation, be treated as trade acceptances when such drafts are accepted by the purchaser?

It appears that it is customary for the seller of such goods to contract for their installation and to include the cost of installation in the selling price.

In the opinion of the Board such an acceptance would come within the Board's definition of a trade acceptance.

Based on Advertising Space

(*Opinion of Counsel*) *January* 9, 1917

(66) The Federal Reserve Board may properly rule that a draft or bill of exchange drawn by the seller on the purchaser of advertising space and accepted by such purchaser is a trade acceptance.

Acceptances for Advertising

January 23, 1917

(67) The term "goods" as used in the regulations of the Board includes goods, wares, merchandise, or agricultural products, including live stock, and because of the doubts raised as to whether this term is

broad enough to include advertising space, the Board has ruled that a draft or bill of exchange drawn by a publisher, or other advertising agency, on the purchaser of advertising space and accepted by such purchaser shall be considered a trade acceptance, provided the advertisement on which the draft or bill is based is for the purpose of promoting or facilitating the production, manufacture, distribution, or sale of goods, wares, merchandise, or agricultural products, including live stock; and provided further that such advertisement is not illegal and is not for the purpose of promoting or facilitating any transaction which is prohibited by the laws of the State in which it is to be consummated.

Trade Acceptances

(*Federal Reserve Board Ruling*)

(68) A trade acceptance containing the statement that "the obligation of the acceptor hereof arises out of the purchase of goods from the drawer as per invoices, a record of which is given in the subjoined statement," is a valid and desirable acceptance when offered with the "subjoined statement" detached in accordance with directions in the form.

An acceptance to pay at a particular place different from the residence of the acceptor is a general acceptance, unless it expressly states that the bill is to be paid there and not elsewhere, and does not render the bill non-negotiable.

(*Opinion of Counsel*) *December* 20, 1918

(69) An opinion is asked on the following questions:

1. Whether a trade acceptance containing the statement that "the obligation of the acceptor hereof arises out of the purchase of goods from the drawer as per invoices, a record of which is given in the subjoined statement," is a valid and desirable acceptance when offered with the "subjoined statement" detached in accordance with the directions in the form?

2. Should a bank or bill house have any hesitancy now, in view of the variant legal rulings or decisions, in purchasing a bill payable in New York drawn on a firm in Cleveland, without the language suggested by the trade acceptance council to cover this point?

Considering these questions in the foregoing order, (1) Section 3 of the negotiable instruments law provides in part as follows:

"An unqualified order or promise to pay is unconditional within the meaning of this act, though coupled with * * * a statement of the transaction which gives rise to the instrument."

In accordance with this section, it has been held that the words "as per terms of contract," written after the words "valued received" on the face of a promissory note by the maker before it is delivered, do not destroy the negotiability of the note or make its payment to a holder in due course conditional upon the performance of the contract intended to be referred to by the maker.

By analogy, the "subjoined statement" referred to in the case under consideration may be treated as a part of the statement of the transaction giving rise to the draft. Such a statement, under the better authorities, is not an essential part of the draft, and to detach

it should not, therefore, destroy its negotiability. It could not be treated as an unauthorized alteration of the acceptance, because the order of the drawer in the form submitted contains specific authority to "detach this memorandum from the trade acceptance before discounting or depositing it for collection." The drawee, therefore, assents to the order of the drawer, and in the opinion of this office such an acceptance may be treated as negotiable.

The Board has heretofore approved a form of trade acceptance containing the statement that it is drawn "in settlement of the purchase of goods as billed in our invoice No. , dated ."

The same general principles seem to be involved in the present case.

In answer to question (2), this office, in an opinion published in the April, 1917, *Federal Reserve Bulletin*, page 289 (*see par.* 147), reached the conclusion that an acceptance to pay at a particular place different from that named in the draft is a general and not a qualified acceptance unless the acceptor expressly states that the bill will be paid at the place designated by him and not elsewhere.

As some counsel expressed some uncertainty as to the correctness of this view, the trade acceptance counsel recommended that the drawer incorporate in the body of the draft authority for the drawee to make such an acceptance. This would, of course, remove any doubt that may exist on the subject, but after further considering the question involved I am still of the opinion that even without this authority incorporated in the draft the drawee might accept a draft as above outlined without destroying the negotiability of the instrument.

Bills Payable to the Order of the Drawee

(*Opinion of Counsel*) *December* 13, 1917

(70) A bill made payable to the order of the drawee is not negotiable until the drawee as payee has indorsed it. When it has been accepted and indorsed by the drawee it is a valid negotiable instrument in the hands of a third party, and the drawer is not released, since the terms of his order have been specifically complied with.

Indorsement of Acceptances

(*To a Federal Reserve Bank*) *July* 12, 1918

(71) Acceptances must bear the signature in blank or to order of the last party to whom the acceptance has been indorsed, but if the acceptance is indorsed in blank it can, of course, change ownership from one holder to another without being indorsed by each subsequent holder, and the title would pass all the same.

As a matter of better protection, purchasers of acceptances generally have the acceptance indorsed to their order, thus insuring themselves against their being collected or disposed of by others than the legitimate owner. In that case, of course, the holder has to indorse the bill. Where the purchaser is not quite certain as to the genuine character of the signature on the bill, he would, of course, be well advised to insist upon indorsement by the seller.

In England the habit is general to indorse acceptances freely, and, as you know, I am very much in favor of establishing a similar practice here. As a matter of fact, in New York we have progressed so far that out of about $120,000,000 of acceptances held by the New York

Federal Reserve Bank, only about $3,000,000 were unindorsed according to its last statement.

I hope we may soon reach the point when Federal Reserve Banks can make a definite rule not to buy bankers' acceptances except such as bear at least three responsible signatures, being those of the acceptor, the drawer, and the indorser.

Waiver of Demand, Notice and Protest

(*Opinion of Counsel*) *February* 13, 1915

(72) The acceptor of a bill of exchange is the principal debtor. The law requires that notice of demand and protest be given to parties secondarily liable in case of dishonor. This right to receive notice is a personal one which may be waived by the parties entitled thereto—that is, the drawer and indorsers; but such waiver has no effect on the acceptor or principal debtor.

Negotiability of Bills of Exchange

(*Opinion of Counsel*) *April* 13, 1916

(73) Negotiability of a bill of exchange is not affected by provisions which waive demand, notice, and protest; which waive homestead exemption rights; and which provide for the costs of collection* and attorney's fees.

Bills Payable with Attorney's Fees or Collection Charges

(*Opinion of Counsel*) *July* 10, 1918

(74) While a bill containing a provision for payment of the costs of collection and attorney's fees, if it is dishonored at maturity, is a valid negotiable instrument, a bill drawn for a fixed sum "with collection charges" is not a negotiable instrument unless it is so drawn as to show that no collection charges are to be included unless the bill is dishonored at maturity.

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*In the circular letter No. 147, dated February 26, 1919, The Federal Reserve Bank of New York announced the revision of charges on acceptances and enclosed a copy of the by-laws revised by the New York Clearing House.

"Sec. 6. A. On acceptances of banks, bankers, and trust companies taken by member or clearing non-member institutions the charge shall be governed by the "Schedule showing when the proceeds of Bankers' Acceptances will become available," as published by the Federal Reserve Bank of New York from time to time; that is to say, for such items for which credit is available at the Federal Reserve Bank of New York on the day of maturity, the charge shall be discretionary; where credit is available at said bank one or two days after maturity, 1/40 of 1%; where credit is available at said bank three or four days after maturity, 1/20 of 1%; where credit is available at said bank later than four days after maturity, 1/10 of 1%.

B. All notes or other time obligations, not provided for in Sub-division A of this Section, purchased by member or clearing non-member institutions payable elsewhere than in New York City, shall be subject to a charge of not less than 1/10 of 1%, except that in the states of Florida, Louisiana, Mississippi, New Mexico, North Carolina and South Carolina the charge shall be not less than 1/8 of 1%, provided, however, that for notes or other time obligations purchased or discounted by any collecting bank, payable elsewhere than in New York City but with respect to which, the maker, endorser or guarantor; or any bank, banker or trust company maintaining an account with the collecting bank, gives a written agreement at the time of such purchase or discount, that payment is to be provided in New York City on date of maturity in New York funds at par, the charge shall be discretionary."

The Reserve Bank schedule showing when proceeds of bankers' acceptances will be available if collected through the Federal Reserve Bank of New York reads as follows:

"On and after March 1, 1919, bankers' acceptances will be received by the Federal Reserve Bank of New York for collection from its member banks and from Federal Reserve Banks but bankers' acceptances payable at New York Clearing House banks will not be received from Clearing House members.

"By arrangements completed with all other Federal Reserve Banks the proceeds of bankers' acceptances payable in cities where Federal Reserve Banks or their branches are at present or may hereafter be established will be available, subject to payment on day of maturity. (Continued on following page.)

NEGOTIABILITY OF BILLS AND NOTES MADE PAYABLE "IN EXCHANGE"

(Opinion of Counsel) *August* 10, 1916

(75) A bill or note made payable "in exchange" is not payable "in money" and is, therefore, not negotiable. Federal Reserve Banks cannot be required to receive checks and drafts drawn in this manner for collection or credit.

"Proceeds of bankers' acceptances payable elsewhere than in Federal reserve or Federal reserve branch cities will be available, subject to payment, one or more days after maturity, until further notice, in accordance with the following schedule:

	District	Credit Available at Maturity for Items Payable in	Credit for Items Payable Elsewhere in District Available
1.	Boston	Boston, Mass	1 day after maturity.
2.	New York	New York, N. Y. Buffalo, N. Y.	1 day after maturity.
3.	Philadelphia	Philadelphia, Pa	1 day after maturity.
4.	Cleveland	Cleveland, Ohio Cincinnati, Ohio Pittsburgh, Pa.	1 day after maturity.
5.	Richmond	Richmond, Va Baltimore, Md.	2 days after maturity for Maryland, District of Columbia and Virginia. 3 days after maturity for West Virginia, North Carolina and South Carolina.
6.	Atlanta	Atlanta, Ga New Orleans, La. Jacksonville, Fla. Birmingham, Ala	1 day after maturity for acceptances of member banks only. Acceptances of non-members when collected.
7.	Chicago	Chicago, Ill Detroit, Mich.	1 day after maturity.
8.	St. Louis	St. Louis, Mo. Louisville, Ky. Memphis, Tenn. Little Rock, Ark.	1 day after maturity.
9.	Minneapolis	Minneapolis, Minn St. Paul, Minn.	1 day after maturity.
10.	Kansas City	Kansas City, Mo Omaha, Neb. Denver, Col.	1 day after maturity.
11.	Dallas	Dallas, Tex El Paso, Texas.	1 day after maturity.
12.	San Francisco	San Francisco, Cal Spokane, Wash. Portland, Ore. Seattle, Wash. Salt Lake City, Utah	1 day after maturity.

The items to be collected must be received by the collecting Federal Reserve Bank or branch in time for the presentation at maturity to the accepting bank or the bank designated as the place of payment.

Eligibility of Drafts Under Credits

(*Federal Reserve Board Ruling*) *January* 19, 1919

(76) Drafts drawn under the credits opened by certain banks to finance the Cuban sugar crop are eligible for rediscount with a Federal Reserve Bank when accepted by the bank against which they are drawn. In this case the sugar in question was sold to the United States Equalization Board for shipment to the United States or United Kingdom under contract entered into between the purchasers and the Equalization Board through the agents of the former in New York.

Bankers' Acceptances Drawn Against Shipment of Goods from a Corporation to Its Agent

(*To an individual*) *August* 24, 1917

(77) A member bank may properly accept a draft drawn against the shipment of goods from a corporation to its agent or branch even though no sale of the goods is involved in the transaction.

The Federal Reserve Act authorizes any member bank to accept drafts or bills of exchange which grow out of transactions involving the domestic shipment of goods, provided that shipping documents conveying or securing title are attached at the time of acceptance and provided further that such drafts or bills of exchange have a maturity of not more than six months' sight to run, exclusive of days of grace. It is the opinion of the Board, however, that although the Act fixes a maximum maturity of six months, nevertheless, in any case where a draft is drawn against the shipment of goods, in a transaction which does not involve the sale of those goods, the maturity of the draft should approximate the duration of their transit. In such a case the law contemplates that the acceptance of the draft should be for the purpose of financing the shipment and that it should not be the means of furnishing a credit for any other purpose.

A slightly different situation arises, however, in the case where a draft is drawn against the shipment of goods in a transaction involving the sale of those goods, because in that case the draft may properly be drawn and accepted for the purpose of financing not merely the shipment but also the sale of the goods. The maturity of the draft need not necessarily approximate the length of time involved in the shipment in such a case, though it must be limited to a maximum of six months, exclusive of days of grace.

Eligibility of Trade Acceptance for Gas Sold

(*To an Individual*) *April* 23, 1918

(78) Your letter with reference to the eligibility of a trade acceptance given by a gas distributing company to a gas producing company in payment for gas sold, has been considered by the Federal Reserve Board.

The question presented for determination is whether natural gas actually sold and delivered by a distributing company is "goods sold" within the meaning of the Federal Reserve Board's regulations defining a trade acceptance. The Board is of the opinion that an acceptance drawn by a gas producing company on a gas distributing company, and accepted by the latter in payment for the gas sold and delivered,

is a trade acceptance, and that it is eligible for rediscount by a Federal Reserve Bank, provided, of course, it also conforms to the other requirements of the Board's regulations.

Trade Acceptances in Connection With Sales on Installment Plan

(*To an Individual*) *April* 15, 1918

(79) Relative to the use of trade acceptances in connection with the sale of coffee mills, etc., on an installment plan, the counsel of the Board reports as follows:

"If the purchaser is willing to accept the draft in advance of the delivery of the goods, there would seem to be no reason why such an acceptance should not be treated on the same basis as a bill drawn and accepted after delivery of such goods."

A memorandum presented to the Board on the same subject contains the following paragraph, which is herewith transmitted as the expression of the Board's views on this question:

"After the machines have been made and delivered to the customer, and after the seller has been notified by the customer of the delivery, then the seller fills in his name on the acceptances as drawer, and also fills in the date of maturity, . . . the total installment acceptances amounting to the agreed price. None of these acceptances could be negotiated, nor, in fact, is an acceptance at all until after the machine has been delivered and accepted by the purchaser. It would seem . . . that this is clearly a case of a trade acceptance and should be entitled to preferential rates as such."

Sales Corporations

(*Opinion of Counsel*) *December* 12, 1917

(80) A draft drawn by a lumber corporation upon a sales corporation which it and a number of other lumber concerns have organized will, when accepted, become a trade acceptance, even though the selling corporation is a stockholder of the sales corporation, provided the latter is organized in good faith and not merely to act as an agent for the purpose of evading the law.

Drafts Drawn to Finance Sales to the United States Government

(*Opinion of Counsel*) *November* 30, 1917

(81) Drafts drawn in connection with sales to the United States Government of lumber or other material cannot be treated as bills of exchange drawn against actually existing value and are subject to the limitations of section 5200, Revised Statutes, when discounted by national banks. Such drafts do not conform to the requirements of commodity paper as defined by the Federal Reserve Board and should not be discounted at the rate prescribed for such paper.

Acceptances

(*To a Member Bank*) *February* 19, 1917

(82) You ask me for a letter that would guide you in your efforts to finance the cotton business of your clients by acceptances, and you wish me to illustrate, step by step, how I would do it if I were president of your bank, with a capital and surplus of $300,000, in handling acceptances for a cotton firm to the amount of, say, $100,000.

If the financing of this one firm to the extent of $100,000 were your only problem there would be no difficulty at all. Your customer —let me call him Smith for the sake of convenience—would draw upon you at 90 days' sight, securing you by the pledge of cotton properly stored in a warehouse independent of himself. Smith would then proceed to sell this acceptance, which he could do either by going to a local bank in your city or you could send it for him to a St. Louis bank, or to the Federal Reserve Bank in St. Louis, which would buy your acceptance, provided your bank commands a sufficient credit, at the rate for private discounts—at present about 3½ per cent. Inasmuch as you accept for one borrower in excess of 10 per cent. of your capital and surplus you could not yourself buy the paper from your customer, because, in that case, you would be making him a loan and the 10 per cent. limit would apply. (See Federal Reserve Bulletin, December, 1916, p. 682) (*see par.* 168). The total limit up to which your bank can accept is $150,000, and inasmuch as there are, I suppose, other customers in addition to Smith for whom you wish to undertake to finance cotton holdings, I suggest that you arrange with a bank having a greater capital and surplus, either in St. Louis or elsewhere, to participate with you in any large acceptance proposition which presents itself. For instance, take the case of Smith. You might properly accept for $30,000 and let the bank with which you have an arrangement accept for the balance of the $100,000, authorizing you to act as its agent in holding and supervising the collateral security after acceptance and compensating you for that service.

Contract Not Fulfilled

December 10, 1915

(83) A member bank would be justified, if fully secured, in accepting drafts drawn by a local cotton-buying firm having a contract to sell to foreign buyers if the transaction, after having been made in good faith, ultimately resulted in the sale of the cotton to an American instead of a foreign purchaser. It was assumed in connection with this interpretation of section 13 that the bank had received permission from the Board to accept drafts or bills of exchange drawn upon it; that the cotton buyers had a contract to sell cotton to a firm of Liverpool; that they held the cotton subject to shipping receipt of the Liverpool firm and that because of freight rates and shipping conditions the Liverpool firm changed its policy and directed the sale of the cotton.

Drafts Growing Out of Transactions Involving the Importation or Exportation of Goods

(*Opinion of Counsel*) *September* 16, 1918

(84) Drafts drawn under an agreement whereby the drawer agrees to manufacture and import into the United States in time to meet the maturity of such drafts certain products which shall have been sold by the shipper and are to be ready for immediate delivery and consigned to a firm of bankers procuring the acceptance of such drafts for the drawer are not eligible for acceptance by member banks; since they do not grow out of "transactions involving the importation or exportation of goods" within the meaning of section 13 of the Federal Reserve Act.

Bankers' Export Acceptances Defined

(*Opinion of Counsel*) *April* 1, 1918

(85) Where a dealer who is engaged in the purchase of the same character and class of goods for export and for domestic use desires to finance the purchase and sale of goods to be exported, his agreement with a member bank accepting such drafts should show that he has a contract for the export of the goods; that the total amount of drafts drawn under such credit will not exceed the aggregate amount involved in the export transaction; that the proceeds of the drafts are to be used in connection with the export transaction; and that the proceeds of the sale of the goods exported will be applied in payment of the acceptances unless the dealer has in the meantime placed the bank in funds to meet them at maturity, or has secured such acceptances in the manner required of domestic acceptances.

Based on Importation or Exportation of Goods

March 24, 1917

(86) Your letter submitting an inquiry of one of your member banks as to whether or not it could accept clean drafts drawn by an exporter in Chile for the purpose of providing funds with which to purchase beans, peas, etc., from farmers in Chile, has been received.

Unless the Chilean exporter is under contract to ship the peas, beans, etc., purchased from the farmers in that country, to some other country, and the member bank has a guarantee to this effect, the transaction would not seem to be one which involves the importation or exportation of goods.

The mere fact that the Chilean exporter intends to sell these goods in a foreign country would not be sufficient, but there must exist some actual contract of sale, and it must appear that the drafts in question are merely drawn in advance of the actual shipment of goods under contract of sale.

Not Eligible for Acceptance

December 8, 1916.

(87) You state that an acceptance house which has purchased an acceptance based on the importation or exportation of goods desires to reimburse itself by drawing a bill upon a national bank, pledging as collateral security for the bill the acceptance which was based upon the transaction involving the importation or exportation of goods. You ask whether a national bank would be authorized to accept a bill of this character under the provisions of Section 13 of the Federal Reserve Act.

That section authorizes national banks to accept drafts or bills growing out of transactions involving the importation or exportation of goods, and, though the Board has ruled that it is not essential that the specific goods be identified or even in existence at the time of the acceptance in order to make it legal, nevertheless that acceptance must grow out of a specific transaction which itself involves the importation or exportation of goods.

In the case presented in your letter the acceptance house has purchased with its own funds an acceptance based on the importation

or exportation of goods. That acceptance necessarily must have grown out of a transaction involving the importation or exportation of goods, but it is the opinion of the Board that there is no direct or logical relation between that transaction and the subsequent one in which the purchaser of that acceptance arranges before its maturity to reimburse himself by drawing a new bill secured by the first acceptance. The new bill cannot properly be said to grow out of the original export transaction in the sense contemplated by the Act. If that was so, it would be possible to have two or even more acceptances drawn for the same amount and existing at the same time, purporting to finance the same export transaction. It is obvious that the law did not contemplate pyramiding acceptance credits in that manner.

The Board believes, therefore, that no national bank can legally accept a draft drawn under the circumstances set forth in your letter, first, because it is not an acceptance growing out of a transaction involving the importation or exportation of goods; and second, because it is not an acceptance of the character authorized by the amendment of September 7, 1916. It is not drawn by a bank or banker located in a foreign country, nor does it grow out of a transaction involving the domestic shipment or storage of goods.

Acceptances in Domestic or Foreign Transactions

(*To a Federal Reserve Bank*) *April* 10, 1918.

(88) It appears that the ——— certifies that a draft drawn by it against the ——— was drawn for the purpose of financing the sale to the Allied Purchasing Commissions of packing-house products contracted for export to Europe. You ask whether this can be treated as a banker's acceptance against goods for export. It is assumed that the firm of ——— has no contract to export, and that its transaction is completed when its sale is made to the Allied Purchasing Commission.

This case appears to be covered by the following opinion of counsel: "A transaction in order to be the basis of a draft or bill eligible for acceptance by a member bank must itself involve the importation or exportation of goods. A transaction, wholly independent of the transaction covering the importation or exportation of goods, is not sufficient basis for an acceptance under the terms of section 13."

In each of the cases submitted by you it appears that the contract between the seller of the goods who draws the draft and the purchaser is entirely independent of the contract for the export of the goods. This being true, the draft would have to be treated as drawn in a domestic transaction, and the drafts should be accompanied by shipping documents or secured by warehouse receipts or other similar documents conveying and securing title when accepted by the drawee bank.

A different situation would, of course, be presented if the drawee bank accepted the drafts at the instance of the purchaser of the goods, the purchaser having a contract to export such goods. In such case, the drafts would grow out of a transaction involving the export of the goods and could be accepted by the drawee bank under authority of section 13 of the Federal Reserve Act.

Drafts Drawn for the Purpose of Financing Sale of Goods to Allied Purchasing Commissions

(*To an Individual*) *October* 19, 1917.

(89) I wish to acknowledge receipt of your letter relating to the right of a member bank to accept drafts drawn for the purpose of financing the sale of goods to one of the allied purchasing commissions, such goods to be delivered aboard ship and paid for within a reasonable time thereafter.

Section 13 of the Federal Reserve Act authorizes any member bank to accept drafts or bills of exchange "growing out of transactions involving the importation or exportation of goods." The Board believes that the sale of goods to be exported by the purchaser in the manner indicated in your letter comes within the terms of that section, even though the title to the goods be transferred to the foreign purchaser before the shipment out of the United States actually begins. The transaction against which the draft is drawn involves the direct sale to a foreign purchaser, and the fact that the sale itself may be consummated before the exportation of the goods actually commences is immaterial, provided, of course, that the transaction is bona fide and that the accepting bank has no reason to believe that the purchaser will divert the goods from their foreign destination.

It may be mentioned in this connection that even if this transaction did not involve the exportation of goods a member bank might accept a draft drawn for the purpose of financing it if it involved a domestic shipment of goods and if the shipping documents are attached at the time of acceptance. An acceptance of that character would seem to be permissible in any case where the goods are shipped from the interior of the seaboard preparatory to exportation.

Drawn to Finance the Future Importation of Goods

June 14, 1917.

(90) The Board is of the opinion that a national bank may properly accept a draft drawn for the purpose of importing goods, whether or not the sale of the goods under consideration has actually been consummated at the time of the acceptance of the draft. If the accepting bank is assured that the proceeds of the draft will ultimately be used solely for the purpose of financing a transaction involving the importation of goods, it is immaterial whether or not the goods have actually been sold at the time of acceptance. In fact, it is not even necessary that the goods to be sold be identified at the time of acceptance. The accepting bank, however, must be reasonably sure that the draft is drawn for the purpose of financing a transaction involving the importation or exportation of goods, and that its proceeds will be used for that purpose.

Advances on Cotton for Export

August 5, 1916.

(91) Section 13 of the Federal Reserve Act construed to justify a national bank in accepting a draft drawn upon it in settlement of advances for cotton being accumulated by cotton buyers for export. The fact that there is a temporary delay in actual shipment of goods is immaterial.

Identification of Specific Goods

November 9, 1915.

(92) It is not necessary that the specific goods covered by an acceptance based upon an import or export transaction be identified at the time of the acceptance. In fact, the goods may be purchased and shipped subsequent to the time of the first acceptance; provided, however, there is a definite, bona fide contract for the shipment of the goods involved within a specified and reasonable time.

Good faith must be relied upon to a large extent in determining whether an acceptance is based upon a transaction involving the importation or exportation of goods.

Statement Form

December 16, 1915.

(93) Announcement that the Federal Reserve Board will require statements satisfactory to it in connection with acceptances held to mean that the statement shall be satisfactory in form.

Banks May Ask Assurances

November 9, 1915.

(94) Member banks may best protect themselves in determining whether acceptances are based upon the exportation or importation of goods by stipulating the right at times to ask for substantiation of assurances from a customer.

Evidence from State Member Banks

November 9, 1915.

(95) Federal Reserve Bank reserves the right to ask State member banks for evidence underlying the certification given it as to an acceptance.

Acceptance by Member Banks of Drafts Drawn in Transactions Involving Export of Goods

(*Opinion of Counsel*) *April* 11, 1918.

(96) A dealer having drawn drafts accepted by a member bank in an export transaction should be given the option, with the consent of the accepting bank, to secure such drafts in the manner required of those drawn in domestic transactions if he wishes to use the proceeds derived from the sale of the goods exported for purposes other than the payment of such acceptances.

Bankers' Acceptances Against Open Accounts of Foreign Purchases

(Opinion of Counsel) *January* 29, 1919.

(96A) "We should like to have your opinion and advice as to a certain method of financing export business, which has been proposed to us by one of our good customers, who are of unquestioned standing.

"The company in question finds that competition, particularly with European sellers, is compelling them to refrain from drawing drafts, either sight or time, against shipments to certain big buyers abroad. These buyers insist on having goods sent to them on open account, and as the terms are frequently as long as 90 days, or even 4 months, it means that for a South American shipment a delay of 6 or 7 months can easily elapse from time of shipment from New York to receipt of proceeds in New York, even when the bill is paid without extension of original terms. To help him finance such a class of business, he proposes that at regular intervals (to illustrate, once a week) he will exhibit duplicate invoices and duplicate documents, showing shipments actually made during the past week, and ask us to accept his time draft on us, for 90 days, with privilege of one or two renewals, if necessary, to aid him in carrying the load on these exports until returns are received."

The question to be determined is whether drafts drawn under the foregoing circumstances may be treated as growing out of a transaction involving the importation or exportation of goods?

Although it is clear that there has been an exportation of goods, it does not appear that the drafts in question can be said to have grown out of the transaction which involved the exportation, within the meaning of the act.

As previously pointed out the language used in the act is broad enough to vest in the Board a wide discretion to determine how remotely or how directly the drafts drawn must be connected with the transaction involving the exportation. Considering the general purposes of the act, however, it is clearly contemplated that these credits were to be opened for the purpose of facilitating international commerce; that is to say, to enable the parties to the transaction actually to export and sell the goods. It was hardly the intention of Congress to authorize member banks to exercise this power for the purpose of enabling domestic concerns to extend credits on open account to foreign purchasers. In the opinion of this office the approval of this credit would require a forced construction of the provisions of section 13 of the Federal Reserve Act.

Crossties and Lumber Good Security

August 12, 1915.

(97) Bills drawn for the purpose of providing funds to export crossties and lumber to Cuba are eligible for rediscount if properly indorsed, and otherwise conforming to the regulations of the Federal Reserve Board. Such paper, it is presumed, would take the 90-day rate.

December 15, 1916.

(98) There cannot be any objection to permitting the mills to substitute other warehouse receipts for cotton receipts during the life of the acceptance.

The second question, whether receipts must be registered warehouse receipts or receipts of warehouses belonging to the mills receiving the credit, I have to refer you to our letter of Special Instructions No. 2, 1916, in which you will find that we say under "f": "In purchasing or discounting bankers' acceptances or other bills which are secured by warehouse receipts, etc., the Feleral Reserve Banks should make sure that the receipt is issued by a warehouse which is independent of the borrower."

As to your third question, relating to the acceptance of a private banking house made for a bag company, stating in the body of the draft that it is for burlap from Calcutta stored on the docks, I should say that if the credit were granted before the importation took place there would be no objection to continuing or renewing the acceptance while the goods are on the docks. If it is a new transaction entered into after the importation, as such, had been completed, it would be a domestic transaction, and in that case it would be a question whether burlap is to be considered "readily marketable goods"—in which case the acceptor must be secured by warehouse receipts or other documents.

You ask how far you should satisfy yourselves as to the fact of whether or not the acceptor has been secured by such documents. As to that, you must use your own judgment. As written you frequently, we do not want to be too technical, but we must be certain that the law is not being evaded, and you ought to be careful to impress upon the acceptor that the rules must be observed and that from time to time you may have to inquire as to whether this is being done. Generally speaking, if you are dealing with a private firm that you are trusting, and that from time to time must come to you and report to you about its financial condition, you should be in a position to find out for yourself what the methods of the firm are in the acceptance business and how far it would be necessary for you to make further inquiries and investigations to be certain of your ground.

WAREHOUSE RECEIPTS

(*To a Federal Reserve Bank*) *November* 30, 1917.

(99) "With a view to obtaining bank acceptances, some of our mills are taking out registration for their storehouses in their own name, and some others are organizing their clerks and bookkeepers as separate corporations to register. This last is a mere subterfuge, and yet the claim is made that warehouse receipts of the latter are more favorably considered than the first."

You ask to be advised as to the attitude of the Board in this matter. While the Board desires to encourage in every way the creation of a proper discount market for acceptances and the use of this form of negotiable instrument, it desires the banks to carefully observe the spirit as well as the letter of the law in developing this market. The Board has heretofore ruled that warehouse receipts

offered as security for bills accepted by member banks under authority of section 13 of the Federal Reserve Act must be issued by warehouses which are independent of the borrower. It recognizes the separate entity of a corporation issuing the receipt when such corporation is not itself the borrower. Where a corporation is formed, however, as a subterfuge for the purpose of evading the spirit of the Board's ruling, this fact should be taken into consideration by the member bank accepting a bill and by the Federal Reserve Bank to which it is offered for discount.

If the borrower exercises such control over the corporation issuing the warehouse receipt as to give him control over the goods in storage, the purpose of requiring a receipt of the independent warehouseman would be defeated. The corporation issuing such receipt must be organized in good faith as an independent corporation, and its affairs must be administered by duly authorized officers and agents independent of the borrower in order to comply with the rulings of the Board referred to.

Warehouse Receipts as Security

(*To a Federal Reserve Agent*) *July* 29, 1918

(100) "There is no provision of the Federal Reserve Act requiring notes to be secured by warehouse receipts in order to be eligible for rediscount. The writer evidently has in mind the question whether such warehouse receipts would form a sufficient security for drafts drawn against a member bank in a domestic transaction and accepted by the bank.

"The requirements of the Board appear to have been met in that a separate corporation has been created and the receipts are to be issued by that corporation and not by the borrower. I would suggest, however, that as both corporations have practically the same officers, the manager of the warehousing company who executes the receipts should not be an employee of the borrowing company, as the Board requires that the receipts should be issued by a company independent of the borrower, and this requirement should be met in substance as well as in form."

(*To an Individual*) *August* 13, 1918

(101) You refer to the informal ruling of June 10, 1918 (*see par.* 102), which requires that the lessee of warehouse premises be independent of the borrower, and that he have entire control and custody of the goods; that the borrower must not have access to the premises except with the permission of the lessee, and that he shall exercise no control of any sort over the goods against which warehouse receipts are issued.

You state that one of your borrowers, a corporation, proposes to set aside part of its readily marketable goods and materials not necessary for immediate purposes, in a warehouse controlled by a separate corporation engaged solely in the warehouse business, the entire stock of which is owned by the prospective borrower, and that it is your desire to use warehouse receipts issued to the borrower as security for drafts drawn against you and accepted by you in accordance with section 13 of the Federal Reserve Act. You ask if the

conditions of the Board's ruling will be regarded as having been complied with if you should place a custodian or representative of the ——— Company on the premises of the warehouse "who shall have access to the goods, thereby eliminating the borrower from exercising any control whatever, through stock ownership, over the goods against which warehouse receipts are issued."

In the opinion of the Board, the mere fact that a representative of the accepting bank shall have "access" to the goods would not necessarily make the warehouse receipts eligible. If, however, a representative of the ——— Company, the acceptor, is given control of the warehouse in which the goods are stored, under a proper resolution of the directors of the warehouse corporation, the fact that the stock of the corporation is owned by the borrower should not prevent the ——— Company from accepting the draft under the circumstances recited.

The agreement between the directors of the warehouse corporation and the representative of the ——— Company, however, should provide that if by any future action of the stockholders or directors of the warehouse corporation an attempt is made to exercise control over the warehouse, the representative of the acceptor should have the right to remove the goods and to place them in storage elsewhere at the expense of the warehouse corporation.

Warehouse Receipts for Canned Goods as Security

(*To a Member Bank*) *June* 10, 1918.

(102) Your letter in reference to the right of a member bank to accept drafts or bills of exchange drawn against the security of canned goods under circumstances set forth in your letter, has had the attention of the Federal Reserve Board.

It appears that a certain concern engaged in the canned goods business proposes to set aside part of its readily marketable goods and materials not necessary for immediate purposes and to place them in storage with a lessee of part of its premises. The lessee is then to issue warehouse receipts to the owners of the goods, which receipts are to be used as security for drafts drawn against the member bank and accepted by that bank under authority of section 13 of the Federal Reserve Act.

You desire to be informed whether such a plan would, in the opinion of the Federal Reserve Board, meet with the requirements of the statute.

In reply, you are advised that if the premises in question are actually turned over to the lessee under a bona fide lease, the lessee being independent of the borrower and having entire custody and control of the goods, there would seem to be no objection to a member bank accepting drafts drawn against the security of warehouse receipts issued by such lessee. It should, however, be expressly understood and agreed that the borrower shall not have access to the premises except with the permission of the lessee, and that he shall exercise no control of any sort over the goods against which warehouse receipts are issued. The warehouse receipt must, of course, be in form to properly convey and secure title to the bank.

Receipt of Custodian of Wool as Warehouse Receipt

(*To a Federal Reserve Bank*) *June* 3, 1918.

(103) It being understood that wool is stored in buildings under control of custodian entirely independent of borrower, custodian's certificate or receipt, if issued in proper form to convey or secure title, may be treated as a warehouse receipt within the meaning of section 13 of the Federal Reserve Act, and acceptance of member bank under such conditions would be eligible for rediscount.

Acceptance of Drafts Against Sugar in Bond

(*To a Federal Reserve Bank*) *May* 7, 1918.

(104) It is the understanding of this office that sugar referred to is placed in bond under transit entry and warehouse receipt issued by collector in negotiable form, but sugar cannot be withdrawn for domestic sale or consumption without special permission of Treasury Department. Board is of opinion that member banks may legally accept drafts drawn against security of such warehouse receipt properly assigned.

Acceptance of Drafts of Food Administration Grain Corporation

(*Opinion of Counsel*) *September* 16, 1918.

(105) The Federal Reserve Board has authority to permit member banks to accept drafts of the Food Administration Grain Corporation secured by some form of receipt or notation on the draft itself, signed by a trustee holding warehouse receipts covering grain stored in warehouses, identifying it as a draft secured by the grain stored.

Custody of Shipping Documents or Warehouse Receipts

(*From and to an Individual*) *September* 7, 1918.

(106) Section 13 of the Federal Reserve Act provides in part that "any member bank may accept drafts . . . drawn upon it . . . which grow out of transactions involving the domestic shipment of goods, provided shipping documents conveying or securing title are attached at the time of acceptance."

A depositor of this bank purchases from time to time cotton seed at various points in the South and at the time of purchase orders shipment to his mills in that section. He desires to finance these shipments by acceptances to be drawn on us under the above section of the Federal Reserve Act. On account of the location of the mills it is not feasible to send the bills of lading to New York City and have them returned in time to obtain timely delivery of the goods.

Our client suggests that he will hand the bills of lading, on the day the draft is presented to us for acceptance, to our correspondent in the South, who would certify to us by letter or telegram that they are holding such bills of lading for our account.

This seems to comply with the spirit of the law, but we would like the ruling of the Federal Reserve Board before undertaking this business.

September 19, 1917.

(107) The Board agrees in the opinion that "it is entirely consistent with the purposes of the act, and a sufficient compliance with its terms, if shipping documents are in the possession of the bank and the bank

has a lien on the property represented by such documents at the time that such bill is accepted. If placed in the possession of the bank's agent, and under the control of the bank, such documents could clearly be considered as in the possession of the bank. . . . There would seem to be no greater reason for requiring shipping documents or warehouse receipts to be physically attached or fastened to the bill than there is for requiring other documents securing such bill to be attached or fastened." Care should, however, be taken that the documents be held for account of the accepting bank by a third party who is in no way interested in the acceptance transaction. A trust receipt of the party for whom the acceptance is made would not be looked upon with favor by the Board.

TRUST RECEIPTS AS ACTUAL SECURITY FOR ACCEPTANCE TRANSACTIONS

(*Opinion of Counsel*) *October* 12, 1917.

(108) If an acceptance is secured by shipping documents which are surrendered by the acceptor for a trust receipt which permits the purchaser of the goods to retain control of the goods, the accepting bank cannot be said to be secured "by some other actual security," as provided in section 13 of the Federal Reserve Act. A trust receipt, however, which does not permit the purchaser to procure control of the goods may properly be said to be actual security within the meaning of the act.

ACCEPTANCE OF DRAFTS WITH DOCUMENTS ATTACHED

(*Opinion of Counsel*) *September* 14, 1917.

(109) A provision of section 13 which authorizes any member bank to accept drafts based upon the domestic shipment of goods, provided shipping documents are "attached," should not be construed so as to require that the documents be physically fastened to the draft. It is sufficient if the accepting bank has possession of the documents at the time of acceptance.

ACCEPTANCE OF DRAFTS WITH DOCUMENTS ATTACHED

(*Opinion of Counsel*) *January* 13, 1918.

(110) Under the provision of section 13, which authorizes any member bank to accept drafts based upon domestic shipment of goods, provided shipping documents conveying or securing title are attached, such documents must be made out or indorsed so as to convey or secure title to the accepting bank.

ACCEPTANCES WITHOUT DOCUMENTS ATTACHED

(*Opinion of Counsel*) *March* 22, 1918.

(111) The acceptance of a draft by a member bank against an acceptance agreement which purports to assign to the bank certain collateral security, but which does not specifically mention any security as assigned, is an ordinary accommodation acceptance, and is not authorized by law.

RELEASE OF SHIPPING DOCUMENTS UPON ACCEPTANCE OF DRAFT

(*To an Individual*) *May* 31, 1918.

(112) You ask whether it is necessary where a domestic acceptance is based upon a bill of lading that the bank retain the bill of lading or other collateral during the life of the acceptance, or may the bank

release the bill of lading after acceptance; also whether the same rule will apply in case the acceptance is secured by a warehouse receipt.

You are advised that inasmuch as the statute merely requires the accepting bank to be secured in domestic transactions by shipping documents or warehouse receipts at the time of acceptance, the bank would no doubt have the right, if it became necessary to do so, to release either the shipping document or the warehouse receipt, provided the draft or drafts accepted for one person did not exceed 10 per cent of the capital and surplus of the accepting bank. This is a question, however, which should be determined by the bank itself.

It is no doubt necessary in some instances for the bank to release the shipping documents under some agreement with its customer in order that the transaction may be consummated. There would seem to be much less reason for releasing the warehouse receipts, and the banks might very properly adopt the rule not to release warehouse receipts other than in exceptional cases. In any event, this is purely a matter of agreement as between the bank and its customers. The Federal Reserve Bank, in rediscounting such acceptances, may reasonably take into consideration the question whether or not they are secured or unsecured at the time they are offered for rediscount.

Acceptance of Drafts and Bills

(113) Inquiries and applications with respect to the power to accept drafts and bills of exchange, presented to Federal Reserve Board, have raised the question whether the institutions which had been authorized to accept up to 100 per cent prior to the passage of the act of September 7, 1916, from which provision for this acceptance power was inadvertently omitted, would be required to make application over again under the amendments to the Federal Reserve Act adopted June 21, 1917.

It would appear that there is no doubt of the authority of the banks which in the past have been granted acceptance powers to continue to exercise such powers without reapplication involving action of the Board therein. In order to make the situation certain, however, the Board at a meeting held August 9, 1917, adopted the following general resolution:

Be it Resolved, That any member bank which has heretofore applied for and received permission of the Federal Reserve Board to accept drafts and bills of exchange in an amount not to exceed 100 per cent of its capital and surplus, be, and it is hereby, authorized and empowered under the authority of the act of June 21, 1917, to accept up to 100 per cent drafts or bills or exchange drawn upon it having not more than six months' sight to run, exclusive of days of grace, which grow out of transactions involving the importation or exportation of goods or which grow out of transactions involving the domestic shipment of goods, provided shipping documents conveying or securing title are attached at the time of acceptance; or which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples.

The authority herein granted shall be effective from this date,

subject, however, to revocation by the Board at any time, upon 90 days' notice, as to any or all of the banks which are subject to the provisions of this resolution.

Resolved Further, That a copy of this resolution be sent to each bank which has heretofore been granted permission by the Board to accept such drafts and bills of exchange to an amount not to exceed 100 per cent of its capital and surplus.

Acceptance of Drafts by State Bank Members

(*To a State Bank*) *October* 5, 1918.

(114) Receipt is acknowledged of your letter of the 28th in reference to the condition attached to your membership in the Federal Reserve System to the effect "that in no event shall the aggregate amount of domestic acceptance outstanding at one time exceed 50 per cent of the capital and surplus of the bank."

This condition relates to drafts or bills drawn against your bank in domestic transactions and accepted by your bank. It does not relate to drafts drawn by an individual against some other drawee which are accepted by the drawee and discounted by you.

The Federal Reserve Board is without authority to permit a member bank to accept drafts drawn against it in domestic transactions in excess of 50 per cent of the capital and surplus of the accepting bank. It may authorize a member bank to accept drafts up to 100 per cent, which amount may include both those which grow out of transactions involving the exportation or importation of goods and those which grow out of domestic transactions; but the statute limits specifically the amount that may be accepted in domestic transactions to 50 per cent of the capital and surplus of the accepting bank.

Power of Member Banks to Accept Drafts Drawn in Domestic Transactions

(*Federal Reserve Board Ruling*) *February* 20, 1919

(114A) Subject to the limitations prescribed by the Act, member banks are authorized—

(a) To accept drafts or bills of exchange which grow out of transactions involving the domestic shipment of goods, provided shipping documents conveying or securing title are attached *at the time of acceptance.*

(b) To accept drafts or bills of exchange which are secured *at the time of acceptance* by warehouse receipts or other such documents conveying or securing title covering readily marketable staples.

All drafts accepted in domestic transactions must therefore be secured at the time of acceptance either by shipping documents or warehouse receipts or other such documents, as specified in the law. If the aggregate amount of drafts accepted for one person, firm or corporation exceeds a sum equal to ten per cent. of the capital and surplus of the accepting bank, such drafts, whether in a foreign or domestic transaction, must remain secured throughout the life of the draft, since the Act provides that—

"No member bank shall accept, whether in a foreign or domestic transaction, for any one person, . . . to an amount equal at any

time in the aggregate to more than ten percentum of its paid-up and unimpaired capital stock and surplus, unless the bank is secured either by attached documents or by some other actual security growing out of the same transaction as the acceptance."

To give this language any meaning it must be assumed that the accepting bank may, if it chooses, release the security in any case in which the total amount accepted for any one customer does not exceed ten per cent. of its capital stock and surplus. Unless this interpretation is placed upon the statute, the provision just quoted would be meaningless in so far as it relates to domestic transactions, since all drafts accepted in domestic transactions must be secured at the time of acceptance.

In any case, however, where the total amount accepted for any one customer exceeds ten per cent. of the capital stock and surplus of the accepting bank the security legally cannot be released unless some other actual security growing out of the same transaction as the acceptance is substituted therefor. This immediately raises the question as to whether or not the ordinary trust receipt substituted for shipping documents, warehouse receipts, etc., constitutes an actual security such as is required by this provision of the act. In an opinion filed by this office on October 12, 1917, and printed on page 881 of the November, 1917, Bulletin (*see par.* 108), it was stated—

> "that a trust receipt which permits the purchaser of the goods to obtain control of those goods either for milling or other purposes is not an actual security within the meaning of the act, and that, therefore, acceptances secured by such trust receipts come within the 10 per cent. limitation imposed by section 13.
>
> "A different situation results, of course, in any case where the trust receipt is of such character as not to permit the purchaser to gain control of the goods, as where they are held for the account of the acceptor by some person, warehouse or corporation independent of the borrower."

The view expressed in this opinion has been followed by the Federal Reserve Board in various rulings relating not only to the purchaser in a transaction involving a sale, but also to any customer for whom a draft is accepted regardless of whether or not there is an actual sale of the goods covered by the documents attached to the draft.

Member Bank Acceptances

(*Opinion of Counsel*) *July* 25, 1916.

(115) When a member bank purchases its own acceptance before maturity, such acceptance need not be included in the aggregate of acceptances authorized by Section 13.

Limitations on Member Bank Acceptances

(*Opinion of Counsel*) *June* 15, 1917.

(116) The 50 per cent limit imposed upon the amount of drafts which a member bank may accept for the purpose of furnishing dollar exchange is separate and distinct from and not included in the limits imposed by section 13 upon the amount of drafts or bills of exchange drawn against the shipment of goods or against warehouse receipts covering readily marketable staples, which a member bank may accept.

Draft Drawn for Purpose of Creating Dollar Exchange

(To a Federal Reserve Agent) *November* 1, 1918.

(117) The Federal Reserve Board has not rescinded its vote to permit member banks to accept drafts drawn upon them by banks or bankers in any Central or South American country, for the purpose of creating dollar exchange, under the provisions of section 13 of the Federal Reserve Act. The list of countries published in the October BULLETIN is that of the specific countries for which, up to that date, applications had been made (*see foot note to par.* 56). Permission granted to a member bank with respect to any country entitles it to exercise similar accepting powers with respect to all countries that have been or may hereafter be designated by the Board as countries whose usages of trade require the furnishing of dollar exchange.

Acceptances by Correspondents at Request and Under Guarantee of National Banks

(Opinion of Counsel) *March* 7, 1918.

(118) Drafts accepted by foreign correspondents at the request, and under the guarantee of a national bank in the United States, should be reported as a direct liability of such national bank, and should be treated as subject to the limitations imposed by the Federal Reserve Act on the acceptance power of national banks.

Limitations Imposed by Section 13 of Act

(To a Federal Reserve Bank) *March* 13, 1917.

(119) I wish to acknowledge receipt of your letter involving the construction of that part of section 13, which reads as follows:

"No member bank shall accept, whether in a foreign or domestic transaction, for any one person, company, firm, or corporation, to an amount equal at any time in the aggregate to more than 10 per cent of its paid-up and unimpaired capital stock and surplus, unless the bank is secured either by attached documents or by some other actual security, etc."

This clause places a 10 per cent limit upon the amount of acceptances which any member bank might make for any one person, company, firm, or corporation. That limit, however, does not apply if "the bank is secured either by attached documents or by some other actual security growing out of the same transaction as the acceptance." I understand that your construction of this provision is the current one; that is, that if documents which were attached at the time of the acceptance are surrendered, and no other actual security growing out of the same transaction is substituted, then the 10 per cent limit will apply. The accepting bank must remain secured in the manner prescribed during the life of the acceptance, in order to be exempt from the 10 per cent limit.

The only doubtful question is as to what constitutes "some other actual security growing out of the same transaction as the acceptance." Shipping documents accompanying a bill of exchange are ordinarily surrendered upon acceptance, and unless the accepting bank is given some other actual security in their place the 10 per cent limit would apply as soon as the original documents are surrendered. If a warehouse receipt for the goods is given upon the surrender

of the shipping documents the bank would undoubtedly be secured in the manner contemplated by the act, but if an ordinary trust receipt, which enables the purchaser to obtain the goods for his own use, is substituted for those shipping documents, the Board understands that the 10 per cent limit would apply, inasmuch as such a trust receipt would not constitute an "actual security" within the meaning of the section quoted. The 10 per cent limit, however, should not apply in any case where the acceptor is secured by a trust receipt whose terms preclude the possibility of the goods coming into the hands of or under the control of the purchaser, as where the goods are held by some person, firm, or corporation, independent of the purchaser.

There is no doubt, therefore, that in any case where shipping documents or warehouse receipts are held by the acceptor the 10 per cent limit does not apply; so also in any case where the acceptor holds a trust receipt which does not enable the borrower to obtain the goods for his own use the 10 per cent limit does not apply; but in any case where the bank holds merely the ordinary trust receipt which gives it only a lien on the goods in the hands of the purchaser or on their proceeds, the 10 per cent limit should apply.

This question of limiting the right of a member bank to accept is separate and distinct from the limit imposed by section 5200 discussed in the opinion of counsel, November 27, 1916 (*see par.* 122). That opinion holds merely that a member bank may discount trade acceptances without reference to the 10 per cent limit, if they are drawn against actually existing values, but it should not be construed to imply that a member bank might accept, without limit, domestic drafts with shipping documents attached, if such shipping documents are to be surrendered without the substitution of some other actual security growing out of the same transaction.

(*To an Individual*) *March* 21, 1917.

(120) A bank having a capital and surplus of $288,000 may, under the National Bank Act, lend to a customer on his own obligation a sum not to exceed $28,800 (10 per cent of capital and surplus). The bank may, however, in addition to such loan, discount for the same customer (although he may have a direct line of credit in bank up to the 10 per cent limit), bills of exchange drawn against actually existing value, or commercial or business paper actually owned by him. The bank may, therefore, legally discount for the customer bills of exchange drawn by him for the purchase price of commodities sold, and accepted by the drawee; or it may discount for the customer the note of the purchaser if actually owned by him, without reference to the 10 per cent limitations prescribed by section 5200.

A member bank acquiring such acceptances or notes may rediscount them with its Federal Reserve Bank. There is no limitation upon the acceptances, but the notes would be subject to the limitations prescribed by section 13 of the Federal Reserve Act; and the Federal Reserve Bank cannot discount paper bearing the signature of the same borrower in an amount greater than 10 per cent of the capital and surplus of the member bank offering such paper.

Bills of exchange drawn against actually existing value and accepted by the drawee within a reasonable time after the shipment of the goods, may be rediscounted with the Federal Reserve Bank without reference to the limitations imposed by section 13 of the Federal Reserve Act. I am informed by counsel for the Comptroller of the Currency that under the practice followed by his office, bills or notes which are renewed at maturity are not to be treated as bills drawn against actually existing value, or as commercial or business paper owned by the person negotiating them, and that renewals are therefore subject to the limitations of section 5200.

Qualified Acceptances

(*Opinion of Counsel*) *July* 25, 1916.

(121) A bill of exchange drawn payable "at sight" and accepted payable in three months is a qualified or conditional acceptance, and the maker and prior indorsers are released. The instrument, in effect, becomes the promissory note of the acceptor, and would not come within the exception of section 5200 as a "bill of exchange," drawn in good faith against actually existing value.

Bills of Exchange Drawn Against Actually Existing Value

(*Opinion of Counsel*) *November* 27, 1916.

(122) A bill of exchange discounted before acceptance may be said to be drawn against actually existing value, within the meaning of section 13 of the Federal Reserve Act, when, and only when, it is accompanied by shipping documents, warehouse receipts, or other papers, securing title to the goods sold. An accepted bill of exchange, unaccompanied by shipping documents or other such papers, may be considered as drawn against actually existing value if drawn against the drawee at the time of or within a reasonable time after the shipment or delivery of the goods sold. In this latter case there must be reasonable grounds to believe that the goods are in existence in the hands of the drawee either in their orignal form or in the shape of the proceeds of their sale.

Trade Acceptances

(*To a Federal Reserve Bank*) *March* 12, 1917.

(123) You are advised that in accordance with the opinion of counsel, approved by the Board, only those trade acceptances which are drawn at the time of or within a reasonable time after the shipment or delivery of goods sold can be treated as bills of exchange drawn against actually existing value.

A bill drawn for a balance due on open account, of long standing, which is accepted by the debtor, might constitute a trade acceptance, but in order for it to be excepted from the limitations imposed by section 13 of the Federal Reserve Act as a bill drawn against actually existing value it must have been drawn contemporaneously with or within such a reasonable time after the shipment of the goods as to justify the assumption that the goods are in existence in the hands of the drawee in their original form or in the form of proceeds of sale.

As evidence of this fact Federal Reserve Banks might reasonably require such trade acceptances as are offered as "bills of exchange

drawn against actually existing values" to show the date of invoice, so that it may be determined whether or not the account is one of long standing.

Trade Acceptances as Bills of Exchange Drawn Against Actually Existing Values

(*Opinion of Counsel*) *August* 21, 1918.

(124) A trade acceptance may or may not be classified as a bill of exchange drawn against actually existing values.

The distinction is not important in so far as the limitations of section 5200 are concerned, since such a trade acceptance negotiated in good faith by the bona fide owner would be exempt from the limitations of section 5200 as "commercial or business paper actually owned by the person negotiating the same," even if it is not exempt as a "bill of exchange drawn in good faith against actually existing values."

Section 13 of the Federal Reserve Act, however, limits the amount of paper of any one borrower rediscounted for any one bank to 10 per cent of such bank's capital and surplus; and trade acceptances are subject to this limitation unless they can be classified as "bills of exchange drawn against actually existing values."

Bills drawn by the seller against the purchaser and accepted before the sale or delivery of the goods should not be treated as bills drawn against actually existing values, since such goods are not in the possession of the drawee either in the original form or in the shape of the proceeds of their sale; except where the goods have passed out of the possession of the drawer and have been placed in storage, subject to the control or order of the drawee.

Limitations on Loans by Member Banks

(*To an Individual*) *July* 30, 1918.

(125) The law does not require a trade acceptance to be secured by negotiable warehouse receipts or shipping documents when purchased or discounted by a national bank. The Federal Reserve Act, however, requires drafts or bills drawn against a national bank to be so secured if such drafts or bills are accepted by the national bank in a domestic transaction. The acceptance of a draft should not, of course, be confused with the discount of an acceptance. If trade acceptances offered your bank are actually owned by the person offering them for discount they would not be subject to the 10 per cent limitation imposed by section 5200. Of course, if they are discounted for the drawee and not for the bona fide holder, they would be subject to the 10 per cent limit referred to.

Limit on Rediscounts

(*To a Federal Reserve Agent*) *October* 19, 1918.

(126) The recent amendment to section 5200, which authorizes the Comptroller to extend the limit to which a national bank may loan on United States bonds, does not amend section 13 of the Federal Reserve Act, consequently, the Federal Reserve Banks, on rediscounting for member banks, must take care that the aggregate notes, drafts and bills bearing the signature of any one borrower rediscounted for any one bank shall at no time exceed 10 per cent of the capital and sur-

plus of said bank, such restriction not applying to the rediscount of bills of exchange, etc.

In the case of State member banks, the Federal Reserve Banks are governed by the provisions of section 9, and are not "permitted to discount for any State bank or trust company notes, drafts, or bills of exchange of any one borrower who is liable for borrowed money to such State bank or trust company in an amount greater than 10 per cent of the capital and surplus of such State bank or trust company; the discount of bills of exchange drawn against actually existing values . . . not to be considered as borrowed money within the meaning of this section."

ACCEPTANCES IN EXCESS OF 10 PER CENT

(*Federal Reserve Board Ruling*)

(127) The acceptance by a bank of unsecured drafts to an amount exceeding 10 per cent of the capital and surplus of the bank would constitute a violation of the limitation contained in section 13 of the Federal Reserve Act, whether or not the customer of the bank guaranteeing the acceptance is the drawer of the draft, or some other person.

(*Opinion of Counsel*) *December* 23, 1918.

(128) A bank having a capital and surplus of $2,000,000 desires to accept drafts drawn by third parties aggregating more than $200,000, under the guarantee of one of its customers.

Would the acceptance of such drafts constitute a violation of that provision of section 13 of the Federal Reserve Act which provides that—

"No member bank shall accept, whether in a foreign or domestic transaction, for any one person, company, firm, or corporation to an amount equal at any time in the aggregate to more than 10 per centum of its paid-up and unimpaired capital stock and surplus, unless the bank is secured either by attached documents or by some other actual security growing out of the same transaction as the acceptance."

This section prohibits a member bank from accepting for any one person drafts aggregating more than 10 per cent of the capital and surplus. The person who enters into an agreement with the bank to protect it against loss, and to whom the bank lends its credit in the form of an acceptance, is obviously the person referred to in the statute.

Accordingly, in the case presented, unless the drafts are secured as provided by the statute, the acceptance of an amount in excess of 10 per cent of the capital and surplus of the bank would constitute a violation of this provision, whether or not the customer of the bank guaranteeing the acceptance is the drawer of the draft, or some other person.

ACCEPTANCES IN EXCESS OF 10 PER CENT

(*Federal Reserve Board Ruling*) *January* 7, 1919.

(129) A member bank may accept either in a domestic or foreign transaction for one person in an amount in excess of 10 per cent, provided the acceptance remains secured throughout the life of the

draft. It cannot accept in domestic transactions without being secured at the time of acceptance, but may release the security after acceptance, upon the execution of a trust receipt or an agreement by the customer that so much of the proceeds of the sale of the goods covered by the security as may be necessary to pay the draft will be deposited with the accepting bank when available, and will not be used for other purposes.

APPLICATION OF SECTION 5200

January 3, 1916.

(130) The 10 per cent limitation imposed by section 5200 of the Revised Statutes is not intended to apply to the mere acceptance of a bill of exchange, but the provisions of section 5200 would apply to the indebtedness arising between the drawer of the bill and the accepting bank in case the drawer fails to furnish funds with which to meet the acceptance at maturity.

BILLS OF EXCHANGE UNDER SECTION 5200, REVISED STATUTES

(*Opinion of Counsel*) *March* 22, 1916.

(131) An obligation in the form of a bill of exchange which exempts the drawer from liability, and, in fact, does not hold any one but the acceptor liable, is, in substance, a promissory note, and not a bill of exchange. It is, therefore, not entitled to the exemption afforded under the provisions of section 5200, because it is not a "bill of exchange drawn in good faith against actually existing values."

BUSINESS PAPER AND SECTION 5200, REVISED STATUTES

November 4, 1916.

(132) The Board finds it necessary to adhere to its established policy of not making any general ruling on the question how much a bank may invest in any particular security. It held, however, that if a firm is a bona fide owner for value of the acceptances of any particular institution, and such acceptances are sold to or discounted with a member bank, the acceptances could, no doubt, be treated as commercial or business paper actually owned by the party negotiating them, and would therefore be excepted from the limitations of section 5200. In other words, if such paper is in fact commercial or business paper, actually owned by the person negotiating it, it may be disposed of by a member bank, and none of the parties thereto, *i. e.*, either the drawer, acceptor or indorser, would thereby become liable to the member bank for money borrowed, within the meaning of section 5200, and in such cases the member bank could acquire such paper without limit.

LIMITATIONS UNDER SECTION 5200 R. S.

(*To a Federal Reserve Bank*) *February* 8, 1918.

(133) If a national bank has loaned to a single firm or corporation an amount equal to 10 per cent of its capital and surplus, may it, while such loan remains outstanding, accept any drafts drawn by that same corporation?

In an opinion of counsel for the Federal Reserve Board (*see* "Member Bank Acceptances," *par.* 167) the conclusion is reached that the limitations imposed by section 5200 of the Revised Statutes on

the amount of money which may be borrowed by any one firm or corporation from a member bank do not apply to or restrict acceptances by that bank.

The Board is of the opinion, therefore, that where the national bank has already loaned 10 per cent of its capital and surplus to a certain company, it may, while the loan is still outstanding, obligate itself as acceptor on a draft drawn by that same company. The limitations of section 5200 on the amount of money which may be borrowed from a member bank are separate and distinct from and in no way restrict the limitations of section 13 of the Federal Reserve Act on the amount of drafts which a member bank might accept for any one firm or corporation. If, however, the member bank discounts its own acceptance under the foregoing circumstances, it must, as heretofore ruled, treat the transaction as a loan, and not as an acceptance, and could not, in that case, lend to and accept for the same firm in an aggregate amount in excess of the 10 per cent prescribed by section 5200.

Exceptions to Section 5200

May 26, 1916.

(134) The fact that a note or draft discounted by a national bank may be secured by cattle would not of itself bring it within the exceptions to section 5200, Revised Statutes, unless it is commercial or business paper actually owned by the person negotiating the same, or unless it is a bill of exchange drawn in good faith against actually existing values.

Cattle as Readily Marketable Commodity

(*To Federal Reserve Banks*) *March* 29, 1918.

(135) An informal ruling of the Board to the effect that it is the view of the Board that cattle should be considered as a readily marketable commodity and that a Federal Reserve Bank may consider as eligible a banker's acceptance secured by a chattel mortgage on cattle, has apparently been construed to mean that a national bank may accept drafts if secured at the time of acceptance by a chattel mortgage on cattle.

In the particular instance in which this ruling was made the drafts were drawn against a trust company which was not a member of the Federal Reserve system, and the question before the Board was whether or not this banker's acceptance was eligible for discount by a Federal Reserve Bank, and not whether a national bank was authorized to accept drafts or bills of exchange secured by a chattel mortgage. As the language of the ruling is, however, susceptible of this interpretation, the Board desires to correct any misapprehension on the subject, and has ruled that drafts or bills of exchange drawn in domestic transactions against a national bank cannot, under authority of section 13, be accepted when secured by a chattel mortgage on cattle, but only when accompanied by shipping documents, or when secured by a warehouse receipt or other similar documents conveying or securing title to readily marketable staples.

While cattle may be treated as readily marketable staples, a chattel mortgage is not considered a document similar to a warehouse receipt,

since the borrower retains the possession of the goods and conveys to the bank only the legal title.

The Board having reached the conclusion that national banks are not authorized to accept bills secured by chattel mortgages on cattle, deems it advisable that Federal Reserve Banks should consider as ineligible bills drawn against the security of such chattel mortgages, whether accepted by member or non-member banks.

Drafts Secured by Cattle Notes

(*Opinion of Counsel*) *July* 23, 1918.

(136) Member banks are not authorized to accept drafts of a cattle-loan company secured by notes of the owner of the cattle, although such notes may be secured by a chattel mortgage executed by the owner of the cattle to the cattle-loan company, and the notes and chattel mortgage accompany the draft at the time of acceptance.

Acceptances Secured by Chattel Mortgages on Cattle

(*To a Federal Reserve Bank*) *March* 25, 1918.

(137) "May arrangements be made for banks to accept or make acceptances based on chattel mortgages, or so-called cattle loans, with the agreement to renew these acceptances for 90 days two or three times?"

In the opinion of the Board, national banks are not authorized by law to accept drafts or bills that are secured by chattel mortgages on cattle. The Board's counsel says:

"Under the terms of section 13 of the Federal Reserve Act, national banks are permitted to accept drafts in a domestic transaction only when shipping documents conveying or securing title are attached at the time of acceptance, or when such drafts are secured at the time of acceptance by warehouse receipt, or other such document conveying or securing title covering readily marketable staples. In the case under consideration no shipping documents are attached, and in the opinion of this office a chattel mortgage on cattle is not a document similar to a warehouse receipt conveying or securing title to readily marketable staples. In the case of a chattel mortgage the borrower retains possession of the goods and merely vests the legal title as security for the debt."

Use by Commercial Concerns

September 20, 1916.

(138) Knowing the interest you and the governor of your bank have felt in the development of trade acceptance paper, I thought you would be interested in hearing that large commercial concerns in other parts of the country are initiating a practice similar to that of a warehouse and lumber company in your district, of allowing a discount where settlement is made by trade acceptance. I quote for your information from the circular of a New York company which has recently come to hand, as follows:

"Our terms are 1 per cent for cash in 10 days, or 1 per cent for 30 days' trade acceptance, in your option, otherwise strictly net.

"Believing that trade acceptances are of assistance to the buyer and seller alike, we invite our customers to co-operate with us in their use. We offer our regular cash discount to customers who, imme-

diately on receipt of goods, send us their 30-day acceptances on the form attached, which has been approved by the Federal Reserve Banks."

This is the kind of a campaign of education which, as it spreads, will ultimately produce a considerable effect in revising borrowing practices away from one-name paper to the highly desirable trade acceptance.

Basis for Figuring Interest for Discount Transactions

(*To Federal Reserve Banks*) *July* 9, 1918.

(139) It is desirable to maintain uniformity in figuring interest in rediscount transactions between Federal Reserve Banks, and as it has proved most convenient in the purchase of acceptances to use interest tables based on 360 days to the year, the Board has decided that these tables should be used in all rediscount transactions between Federal Reserve Banks, and has therefore revoked its previous ruling that the basis of 365 days to the year should be applied, as announced in its circular letter dated January 31, 1918.

Rates for Domestic Acceptances

January 27, 1916.

(140) Discount rate for bankers' acceptances includes domestic acceptances.

Rate on Paper of Acceptance Corporation

(*To a Federal Reserve Bank*) *May* 31, 1918.

(141) Acceptances of this corporation ought to be dealt with exactly as would be the acceptances of a prime private banker. These acceptance corporations are in the same relation to the Federal Reserve system as the private bankers. They cannot become members, but inasmuch as they expect to give you full information about their own financial standing and the nature of their acceptances, and as they exercise a most important function for the further development of our acceptance business and discount market, their operation ought to be encouraged in every respect.

I do not think, therefore, that it would be proper to discriminate against their acceptances when they reach you properly indorsed by a bank or banker. If they should be offered to you without any indorsement, then indeed I would discriminate against them—at least to the extent of one-fourth per cent in the discount rate, if not more.

I am very anxious to see adopted in growing measure the habit of Federal Reserve Banks to insist upon the third signature for all the acceptances that they buy.

It is, of course, understood that the acceptance corporation will publish its reports, and that you will keep yourself fully advised as to its assets and obligations. That will guide your board of directors in its judgment as to how large an amount of these acceptances it will be willing to take from time to time.

Forward Discount Rates

(*Opinion of Counsel*) *May* 18, 1915.

(142) Federal Reserve Banks may, under the established right to fix discount rates for acceptances or other eligible paper, fix a for-

ward rate; that is, a rate to apply at a future time. Such a rate is calculated to accommodate trade and commerce as required by the Act, and will tend to eliminate speculation due to fluctuating rates.

Discount of Renewals

June 16, 1915.

(143) Acceptance business of Federal Reserve Banks not restricted "to the original transactions only," if transaction has not been liquidated. When first acceptance matures member bank may renew the acceptance, and there is no reason why a Federal Reserve Bank may not discount such renewed acceptance although a Federal Reserve Bank must not engage in advance to make such discount of a renewal.

August, 1915.

(144) A national bank is held to be authorized to enter into an agreement having more than six months to run by the terms of which it obligates itself for a period of time specified in the agreement to accept drafts drawn upon it, provided such drafts grow out of transactions involving the importation or exportation of goods, and that the individual drafts have not more than six months' sight to run. This distinction is emphasized: "While a letter of credit or credit agreement may lawfully be made by a national bank which will extend by its terms for a period exceeding six months, the agreement must not be of such a character as will impose upon the holders of drafts accepted thereunder any obligation to renew such drafts so that the period of acceptance shall exceed six months in duration as to any specified draft.

November 9, 1915.

(145) Upon payment of an acceptance the accepting bank may for a reasonable period accept new drafts for the financing of the original transaction, even after the shipment and delivery of the goods, provided such renewels be stipulated in the original contract as an incidental condition of the transaction of importation or exportation upon which the acceptance is based.

Presentment of Bills for Acceptance

(*Opinion of Counsel*) *October* 17, 1916.

(146) The drawer and indorsers of a bill of exchange made payable on a date specified in the bill are not discharged by a failure to present for acceptance, unless the bill expressly provides that it must be presented for that purpose, or unless it is payable elsewhere than at the residence or place of business of the drawee.

Place of Payment

(*Opinion of Counsel*) *February* 27, 1917.

(147) An acceptance to pay at a particular place different from the residence of the acceptor is a general acceptance, unless it expressly states that the bill is to be paid there and not elsewhere, and does not render the bill non-negotiable.

April 11, 1917.

(148) You ask whether a bank in accepting a draft of its customer may make it payable elsewhere than at its banking house.

Under the opinion given above it would seem that the drawer of the draft might make it payable either at the bank against which

it is drawn, or at some other place, and when accepted it would be payable according to its terms, namely, either at the banking house of the drawee or at the other designated place.

If the terms of the original draft make it payable at the banking house of the drawee, the drawee may nevertheless accept it payable elsewhere—as, for example, at a Federal Reserve Bank—provided the acceptance does not stipulate in terms that it is payable only at the Federal Reserve Bank, and not elsewhere.

Discount of Acceptances Not Paid at Federal Reserve Bank

(To Federal Reserve Banks) *May* 7, 1918.

(149) The discount committee of the Federal Reserve Board has reported that in its opinion, "Federal Reserve Banks should insist that acceptances when due should be paid by checks on the local Federal Reserve Bank, in order that they may be charged to the account of the acceptor on the day of maturity, or else that acceptances should be paid by checks through the clearings. If an arrangement on these lines cannot be perfected Federal Reserve Banks ought to be required to add one day to the actual number of days the acceptance has to run when bought, so as to make up for the loss of interest incurred in collecting in this manner."

This report has been agreed to by the Board, and your bank is requested, in buying acceptances, to charge discount for one additional day, except in cases where satisfactory arrangements are made to make actual cash payment at the Federal Reserve Bank on the day of maturity.

Bills Payable Elsewhere Than in the United States

(To a Federal Reserve Bank) *May* 11, 1918.

(150) I have your letter asking whether or not Federal Reserve Banks are authorized to purchase bankers' acceptances payable elsewhere than in the United States.

You are advised that under regulations of the Federal Reserve Board defining bankers' acceptances, any bill which is payable elsewhere than in the United States would not be eligible for purchase as a bankers' acceptance, under the provisions of regulations A and B, series of 1917 (*see par.* 1-48), even though eligible in all other respects.

The acceptance to which you refer, however, might properly be purchased as a bill of exchange payable in a foreign country in accordance with the provisions of Special Instruction No. 2 of 1916, subsection (b) "Purchase of cable transfers and foreign bills of exchange.

"In order to carry on open-market transactions in cable transfers and foreign bills of exchange (including foreign bankers' acceptances)—that is, payments to be made in, or bills payable in, foreign countries—it will be necessary for Federal Reserve Banks to open accounts with correspondents or establish agencies in foreign countries. Such bills of exchange and foreign acceptances must comply with the applicable requirements of sections 13 and 14. Inasmuch as the law prescribes that these foreign accounts and accounts opened by Federal Reserve Banks for such foreign correspondents or agents are to be

established only with the consent of the Federal Reserve Board, Federal Reserve Banks will be required to communicate with the Federal Reserve Board whenever they are ready to enter these foreign fields.

"The Federal Reserve Board realizes that in dealing in foreign exchange the Federal Reserve Banks must necessarily have wide discretion in determining the rates at which they will buy or sell. It is not necessary that foreign bills shall have been actually accepted at the time of purchase. The Federal Reserve Board, however, will require that unaccepted 'long bills,' payable in foreign countries, when purchased, unless secured by documents, shall bear one satisfactory indorsement other than those of the drawer or acceptor, preferably that of a banker. Federal Reserve Banks should exercise due caution in dealing in foreign bills, and boards of directors should fix a limit within which the acceptances or bills of a single firm may be taken."

Differential as to Acceptances

December 4, 1916.

(151) The Board has been considering for several days the question whether there should be any differential in favor of acceptances of member banks, and has reached the conclusion that while a very decided differential may be inadvisable, there is no objection to a moderate differential, say one-fourth of 1 per cent, to apply between member-bank acceptances and the acceptances of large non-member institutions well known throughout the country and whose acceptances necessarily have a broad market. There will be no inconsistency, of course, in applying a higher differential to the acceptances of smaller and less widely known institutions whose offerings would have a restricted market only. As the Board has already approved a rate of from 2 to 4 per cent. for bankers' acceptances, your directors of course have a liberal margin of discretion in the matter.

Discount of Acceptances Indorsed by Member Banks Located in Another District

(*Opinion of Counsel*) *April* 30, 1915

(152) Federal Reserve Banks may, under the provisions of section 13, discount acceptances based on the importation or exportation of goods, provided they have a maturity at time of discount of not more than three months, and provided further, that they are indorsed by at least one member bank. It is immaterial whether this member bank is located in the district of the Federal Bank which is making the discount or in any other district, the term "member bank" being broad enough to include member banks wherever located.

Such discounts, being made under the provisions of section 13, are eligible as collateral security for Federal reserve notes issued under the provision of section 16.

Trade Acceptance Providing for Discount If Paid at Maturity

(*Opinion of Counsel*) *January* 26, 1918

(153) A trade acceptance which consists of an order to pay a certain amount, which is the amount of the debt minus a discount for prompt

payment at maturity, or, if not paid at maturity, to pay a greater amount, which is the amount of the debt without any discount, is an order to pay a sum certain and is negotiable.

Trade Acceptance Providing for Discount If Paid at Certain Time Before Maturity

(*Opinion of Counsel*) *August* 1, 1918

(154) A trade acceptance providing for a fixed discount, if paid at a certain time before maturity, should not be approved for general use by the Federal Reserve Board.

Trade Acceptance Providing for Extension of Time

(*Opinion of Counsel*) *July* 25, 1918

(155) A note or draft containing a provision for an extension of time should not be approved for general use by the Federal Reserve Board.

Federal Reserve Banks Determine Eligibility

October 8, 1915

(156) Federal Reserve Banks must determine the eligibility of an acceptance.

Eligibility of a Note of an Acceptance House or Broker

(*To a Federal Reserve Bank*) *January* 21, 1918

(157) The note of an acceptance house or broker could not be said to have been used for an industrial, agricultural, or commercial purpose, since the business of such acceptance house or broker is not such as to come within any of these classifications. The fact that the note is secured by eligible paper is immaterial if the proceeds are not used for one of the purposes mentioned.

Eligibility for Rediscount of Member Bank Acceptances

(*Federal Reserve Board Ruling*) *February* 20, 1919

(157A) Under the terms of section 13 any draft or bill of exchange which a member bank has the power to accept under the provisions of that section, is technically eligible for rediscount by a Federal Reserve Bank. This does not mean, however, that Federal Reserve Banks are required by law to rediscount every such acceptance tendered to them for that purpose. In developing a general market for acceptances the Federal Reserve Banks are necessarily called upon to carry a large amount of this class of paper, but it is important that the Federal Reserve Board and the Federal Reserve Banks should take all necessary steps to insure conservatism in the exercise of the acceptance power by member banks. The policy of the Board, therefore, as reflected in its various rulings, has been to caution Federal Reserve Banks that in rediscounting drafts accepted in domestic transactions they should consider, and in many cases investigate, the circumstances under which the draft was accepted in order to determine whether or not the particular transaction complies with the spirit as well as the letter of the statute.

It was in view of this policy that the Federal Reserve Board has consistently refrained from encouraging Federal Reserve Banks to rediscount or purchase warehouse acceptances after the warehouse receipts have been released, though there is nothing in the law which prohibits the rediscount of such acceptances. It is recognized, however, that an unrestricted policy of rediscounting or purchasing such acceptances after the warehouse receipts have been released might very probably lead to an abuse of the domestic acceptance privilege by facilitating the use of the warehouse receipt as a mere cloak for a straight loan in violation of the provisions of Section 5200. It cannot be stated, of course, as a hard and fast rule that the acceptance of a draft secured by a warehouse receipt was not a bona fide transaction merely and solely because the warehouse receipt has been surrendered before the acceptance is presented to the Federal Reserve Bank for rediscount. It should, however, put the bank on notice, and should suggest extreme caution in order to determine whether in fact the acceptance complies in every way with both the letter and spirit of the law. When Congress granted the power to accept drafts in domestic transactions, it clearly intended to facilitate domestic commerce and did not contemplate that this power should be use for the purpose of extending unreasonable lines of credit to individual borrowers in substantial violation of the limitations of Section 5200 of the Revised Statutes. If Congress had intended to give greater latitude to banks under its jurisdiction in the matter of loans of this character a much more direct method would have been to remove or to broaden the limitations of Section 5200.

The Board has recognized the fact, however, that in the ordinary course of business shipping documents securing accepted drafts must be released in order that the customer for whom the draft was accepted may procure the goods represented by such documents. It also recognizes the fact that where such drafts are secured by warehouse receipts it is probable that at some period during the life of the draft it may be necessary for the receipt to be surrendered to the customer for whom the draft is accepted in order that the transaction involved may be consummated. In the case of shipping documents it is ordinarily necessary to release the documents at an earlier period than in the case of warehouse receipts.

In either case, as a matter of policy, the security should not be surrendered by the accepting bank until this becomes necessary in order for the transaction to be consummated, and even when surrendered, banking prudence requires that the bank protect itself by procuring either a trust receipt or a definite agreement on the part of the customer to whom the security is surrendered that the proceeds derived from the sale of the goods represented by the shipping documents or warehouse receipts will be deposited with the accepting bank when available to pay the draft at maturity and will not be used by the customer for other purposes. It should be remembered, however, as previously stated, that in any case where a trust receipt is substituted the ten per cent. limit applies if the trust receipt is such as to give control over the goods to the borrowers or the customer for whom the draft was accepted.

Domestic Bankers' Acceptances

(*Opinion of Counsel*) *April* 21, 1917

(158) A draft drawn by the purchaser of goods against a national bank is not eligible for acceptance by that bank under the provisions of section 13 of the Federal Reserve Act merely because it is secured by a bill of lading covering the goods bought.

Eligibility of Trade Acceptances for Rediscount

(*To a Corporation*) *January* 16, 1918

(159) The Board's conception of the trade acceptance is that it is an instrument which carries upon its face the evidence of the commercial character of the transaction which gave it birth. The finance paper of the ——— Corporation, issued against drafts drawn by it on dealers and placed in trust to secure such paper issued by it in the shape of notes or certificates, gives no indication whatever as to the nature of the security, which may or may not be eligible paper. The Board does not concur in your opinion that the statute is satisfied "when the proceeds of a note are used for a commercial purpose, regardless of whether or not the maker of the note is the purchaser of the goods or whether in substance the maker of the note is extending credit to the actual purchaser," etc., for if the maker of the note in the case cited is extending credit to the actual purchaser, it necessarily follows that the ——— Corporation is not itself the actual purchaser but is lending its funds to the purchaser to pay the purchase price. If such a transaction conforms to the statute, then any bank could borrow money and lend the proceeds of its note to a customer who would use such proceeds for a commercial purpose, and then set up the claim that its own note would thereby become eligible for rediscount.

It appears to the Board that the ——— Corporation by issuing notes of this character is really raising money for capital requirements for similar transactions in the future, and that the whole plan is in essence a finance operation rather than a commercial transaction.

Paper for Rediscount

April 19, 1917

(160) Section 13 of the Federal Reserve Act provides that a bill, in order to be eligible for rediscount by a Federal Reserve Bank, must have a maturiity at the time of discount of not more than 90 days. The Federal Reserve Board has, therefore, ruled that a demand note or bill is not eligible under the provisions of the Act, since it is not in terms payable within the prescribed 90 days, but, at the option of the holder, may not be presented for payment until after that time. The trade acceptance submitted by you would very probably be construed by the courts to be a demand bill, since no definite maturity is fixed. It merely states that "in the ordinary course of business presentment will be made 60 days from date," but the holder is not required to present it within that time.

If the bill were altered so as to read "on or before 60 days from date pay to the order of ourselves," etc., it would come within the terms of the law and would be eligible for rediscount. In such case the holder would have the right to present it for payment before the

expiration of 60 days, but could not defer presentment until after that time without releasing the indorsers.

There may be some doubt about the correctness of the statement in your form that the obligation of the acceptor arises out of the purchase of goods if it is intended to have that acceptance cover future purchases. The bill, in order to be a trade acceptance, must arise out of the purchase of goods, and unless that purchase is either consummated or actually contracted for at the time the bill is drawn it is doubtful whether you can properly say that the obligation arises out of the purchase of goods.

Trade Acceptance

October 26, 1915

(161) Tentatively held that a 90-day sight draft drawn by a firm in Calcutta on a company in Boston and accepted by that firm, covering a transaction involving the transportation of merchandise from Calcutta to Honolulu, is a trade acceptance rather than a banker's acceptance. Ruling based upon facts submitted and subject to local conditions.

Drafts Drawn "On or Before 90 Days After Sight"

(*To a Federal Reserve Bank*) *November* 5, 1917

(162) I have your letter inclosing a letter from the ——— Bank in regard to bills drawn "on or before 90 days after sight."

I agree with you that we should not encourage or countenance this practice. If the bank accepts, it ought to accept for a definite period, otherwise the acceptance becomes in effect a limited demand note, or rather a certified check to be presented within a limited period of time. If an acceptance of this kind passed into the hands of a third party (other than the acceptor or the drawer), this third party could then, according to his own requirements, present this note for payment on any day he pleased, and probably the acceptor could not be put in funds in time. There may be conditions where the drawer —the goods being still in course of transportation—would not be in a position to cover the acceptor, even when requested by the latter to do so.

All that is required, I believe, is an understanding with the Federal Reserve Bank that it would permit the acceptor to take up its acceptance before maturity under rebate, and if a Federal Reserve Bank wants to encourage his business there is no reason why the Federal Reserve Bank could not make such an arrangement. But any such agreement would be a voluntary one between a holder of the acceptance and the acceptor and could not affect a fourth party who might happen to become the holder of the acceptance.

Rediscount of Draft for Railroad Supplies

(*Opinion of Counsel*) *August* 14, 1918

(163) Where a railroad company purchasing supplies accepts the draft of the seller and the seller or a third party to whom the draft is sold in good faith discounts it with a member bank, such draft is eligible for rediscount with a Federal Reserve Bank.

Purchase of Acceptances

November 23, 1916

(164) Receipt is acknowledged of your letter inclosing statement of condition of a bank in New Orleans, which institution desires to offer its acceptances to the branch bank at New Orleans.

The Federal Reserve Board has no objection to your bank's authorizing the purchase of the acceptances of this institution by the branch bank at New Orleans, but would like to be advised, as a matter of information, as to the character of the acceptances to be offered—will they be against imports or exports, or will they be against domestic transactions, or both?

Acceptances of Member Banks

(*Opinion of Counsel*) *July* 26, 1917

(165) An acceptance which has been purchased by the accepting bank and subsequently rediscounted with its Federal Reserve Bank is not subject to the limitations of section 5200 of the Revised Statutes.

Purchasing Bank's Own Acceptances

(*To a Federal Reserve Bank*) *August* 1, 1917

(166) While the Board has ruled that when a bank buys its own acceptances they are to be regarded as loans subject to the limitations of section 5200, the right of the bank to resell or reissue the acceptances is, in the opinion of counsel, fully recognized by the authorities, and where this is done they may be treated as acceptances outstanding and not as loans. This would be applicable to cases where the acceptances are sold to or rediscounted with a Federal Reserve Bank as well as to those cases where such acceptances are sold in the open market.

Purchase of Bank's Own Acceptances

November 23, 1916

(167) The attention of the Board has been called to the fact that in some cases member banks, which are authorized under the amendment to the Federal Reserve Act of September 7, 1916, to accept against domestic transactions to the extent of 50 per cent. of their capital and surplus, have been extending credits in this way and have been purchasing their own acceptances, under the impression that by this means they could extend credits to a single borrower up to one-half of their capital and surplus instead of being restricted to 10 per cent. as provided by section 5200, R. S. This question has been carefully considered by counsel, and the Board has ruled that a member bank's own acceptances purchased by it, must be treated as loans and as such are subject to the 10 per cent. limitation. The opinion of counsel will be published in the December issue of the Federal Reserve Bulletin (*extract of this opinion follows this letter*), and in the meantime you are requested to correct any misapprehensions that your member banks may entertain on this subject.

Member Bank Acceptances

(*Opinion of Counsel*) *October* 27, 1916

(168) (a) The limitations imposed by section 5202, Revised Statutes,

on the liabilities incurred by any national bank do not apply to acceptances of such banks.

(b) A member bank may legally purchase its own acceptances, but such a transaction is equivalent to a loan or advance to the customer for whom the acceptance was made and the liability of such customer becomes subject to the limitations of section 5200, Revised Statutes.

(c) The limitations imposed by section 5200, Revised Statutes, on the amount of money which may be borrowed by any individual from a member bank do not apply to acceptances of such bank.

(d) The power of member banks to accept drafts or bills of exchange should not be confused with the power to discount the acceptances of others.

Acceptances Against Bullion

December 4, 1916

(169) The Board has considered your letter with reference to shipment of gold bars to Peru, and has reached the conclusion that gold bars may be properly considered as goods, and that accordingly sixty-day bills when accepted by banks and bankers against such a shipment would be eligible for purchase by Federal Reserve Banks as based upon or involving the exportation of goods.

Bill of Exchange Drawn by the Drawee

(*Opinion of Counsel*) *August* 2, 1916

(170) An instrument in the form of a bill of exchange drawn by an agent of a corporation upon the corporation itself is not a bill of exchange such as is eligible for purchase in the open market by Federal Reserve Banks.

Bills Drawn in Foreign Countries

January 21, 1916

(171) Federal Reserve Banks may buy bills of exchange drawn in foreign countries on American acceptors where in case it is impossible to obtain information from the acceptor or drawer a satisfactory statement from the indorsing bank or banker as to financial condition is obtained.

Promissory Notes Not Eligible

October 8, 1915

(172) As to open-market operations, the Board has reached the conclusion that Congress drew a distinction in sections 13 and 14 between the several forms of commercial paper, and that promissory notes, even though bearing an additional indorsement, must be regarded as excluded from open-market purchases under section 14. There remained, then, as eligible for purchase under this section "cable transfers" and "bills of exchange" of two kinds: (1) So-called foreign bills of exchange, and (2) domestic acceptances drawn by one party on another, as by a seller of goods upon the purchaser, such as have been classified by the Board as trade acceptances either accepted or not accepted at the time of purchase.

Decision as to whether banks should engage in such open-market

operations rests entirely with them and not with the Federal Reserve Board.

The Board leaves to each Federal Reserve Bank the authority granted under section 14 with respect to bills of exchange without restricting regulations.

Banks are cautioned that no bill be bought in the open market which, even if indorsed by a member bank, would be ineligible for rediscount under section 13.

Single Name Paper

(*Opinion of Counsel*) *October* 8, 1915

(173) Any Federal Reserve Bank may, under the provisions of section 14 of the Federal Reserve Act, purchase acceptances and bills of exchange of certain kinds and maturities in the open market, but promissory notes as distinguished from bills of exchange, whether one or more names, are not eligible for such purchase.

Non-Member Trust Company Acceptances Ineligible

January 8, 1916

(174) Acceptances drawn by a manufacturer on and accepted by a trust company not a member of the Federal Reserve System, the proceeds of which are to be used for purchases of raw material and payment for labor where the goods had not been sold and no warehouse receipts or other instruments could be furnished, are held not to be eligible for purchase by a Federal Reserve Bank.

Banker's Acceptance Secured by Bill of Sale

(*Opinion of Counsel*) *November* 4, 1916

(175) A banker's acceptance drawn for the purpose of purchasing goods secured by a bill of sale of stock in hand is not eligible for purchase by Federal Reserve Banks.

Stamp "Trade Acceptance" Has No Value

February 1, 1916

(176) The fact that a loan company has stamped a bill a trade acceptance and signed as "acceptor" does not in itself make it a trade acceptance and is not eligible for purchase as a trade acceptance.

Must Be Accepted by Drawee

February 1, 1916

(177) A draft to be eligible as an acceptance must be accepted by the drawee and not by anyone else. A draft drawn by a corporation cannot be purchased by a Federal Reserve Bank in the open market as a banker's acceptance. For the same reason such a draft is ineligible as a trade acceptance.

Responsibility With Federal Reserve Banks

December 16, 1915

(178) Ultimate responsibility in purchasing acceptances held to rest with Federal Reserve Banks.

Purchase of "Finance Bills" by Federal Reserve Bank

(*To a Federal Reserve Agent*) *October* 22, 1918

(179) You ask for ruling of the Board on the question whether you are authorized to discount or purchase acceptances "drawn by ———, Argentina, at 90 days, in favor of ———, and accepted by the ——— Company, payable in New York."

You state that you are advised that these are finance bills, not having been secured at the time of acceptance by merchandise.

While it is not necessary for a draft drawn in a transaction involving the importation or exportation of goods to be secured by merchandise at the time of acceptance, if these drafts are finance bills they would not be eligible for purchase or rediscount by a Federal Reserve Bank. Section 13 specifically provides that bills of exchange which may be discounted must be issued or drawn for agricultural, industrial, or commercial purposes, or that the proceeds of such bills must have been used or must be intended for use of one of such purposes.

Section 14, which authorizes the purchase of such bills in the open market, specifies that they must arise out of commercial transactions as hereinbefore defined.

If you are satisfied, therefore, that these bills were not drawn for an agricultural, industrial, or commercial purpose, you are correct in your position that they are not eligible for rediscount or purchase by your bank.

War Stamp Taxes

March 26, 1918

(180) The following is a reprint of Treasury decision (T. D. 2682) relating to war stamp taxes on negotiable instruments:

The stamp tax on drafts and checks imposed by Schedule A of Title VIII of the act of October 3, 1917, attaches to drafts or checks (1) at the time of delivery, if (2) delivered within the territorial jurisdiction of the United States, and (3) expressed to be payable otherwise than at sight or on demand, but not to drafts or checks not yet delivered, or delivered in a foreign country, or expressed to be payable at sight or on demand.

Schedule A of Title VIII imposes a tax on—

"6. Drafts or checks payable otherwise than at sight or on demand." By section 800 of the act the tax is payable in respect of such drafts and checks, or in respect of the paper upon which they are written, by any person who makes, signs, or issues the same, or for whose use or benefit the same are made, signed, or issued. By section 802 anyone is guilty of a misdemeanor who "(a) makes, signs, issues, or accepts, or causes to be made, signed, issued, or accepted, any instrument, document, or paper of any kind or description whatsoever without the full amount of tax thereon being duly paid."

(1) The general rule is that a taxable draft or check becomes subject to the tax concurrently with its delivery. In the case of a draft the rule means that the tax attaches, not when it is signed by the drawer, or presented to the drawee for acceptance, or accepted by him, but when it is delivered to the payee, if drawn to a third person, or negotiated by the drawer, if drawn to his order, whether such delivery or negotiation takes places before or after acceptance.

If a draft was drawn and accepted before the passage of the act, but not delivered or negotiated until afterwards, the tax is payable. If a draft is presented to the drawee for acceptance and discount by him, stamps must first be affixed by the drawer, for the acceptance and delivery are simultaneous.

The payee or indorsee from the drawer must see to it that the drawer, as the person "who makes, signs, or issues" the draft, pays the tax before delivery. "Accept" is used in the penal provision in section 802 in the general sense of "receive," not in the special sense peculiar to drafts. No drawee accepting an unstamped undelivered draft would violate the law; but if the draft has already become taxable because of a prior delivery, the acceptor must be sure that the stamps are affixed.

(2) The general rule is that a taxable draft or check becomes subject to the tax if delivered within the territorial jurisdiction of the United States. The rule means that the tax does not attach to a draft drawn and accepted here, but delivered abroad, whether before or after acceptance, but does attach to a draft delivered here, whether before or after acceptance, although drawn and accepted abroad. In general, a draft sent through the mail is delivered when and where deposited in the mail addressed to the payee or the indorsee from the drawer.

If a draft drawn abroad, on a foreign drawee, with a foreign payee, passes through a bank here in the course of collection, no tax is payable, unless it should be delivered by an agent of the drawer to an agent of the payee within the United States. Because of the constitutional restriction that no tax or duty shall be laid on articles exported from any State, drafts with bill of lading attached covering goods in the course of exportation are not subject to the tax.

(3) The general rule is that a draft or check delivered within the United States is subject to the tax if expressed to be payable otherwise than at sight or on demand.

Accordingly, an ordinary sight draft with bill of lading attached is not taxable, but a draft expressed to be payable at sight "on arrival of car," or containing a memorandum to hold until arrival of car, is. A sight draft, accompanied by instructions outside the instrument, as "Do not present until arrival of car," or some such memorandum, is not taxable. A sight draft accepted and paid for the drawee by the collecting bank, which holds it and charges interest until the drawee takes it up, is not taxable.

A draft might be drawn stating no time for payment, which would class it as a sight draft, and be accepted at 90 days, which would change its nature. If negotiated or delivered before acceptance the holder would be obliged to stamp it on acceptance, in default of which both he and the acceptor would be liable for the statutory penalty.

For the purposes of the tax there is no difference in the treatment of ordinary bills of exchange, trade acceptances, and bankers' acceptances, as defined by the regulations of the Federal Reserve Board.

Stamp Tax on Acceptances

(*To a Federal Reserve Agent*) *November* 13, 1917

(181) With reference to your telegram of November 8, reading as follows:

"Are acceptances originating outside but payable inside this country subject to stamp taxes?"

"Are acceptances originating inside but payable outside subject to stamp taxes?"

I beg to advise that the matter was referred to the Board's counsel for a ruling, which he has rendered as follows:

"In my opinion questions should be answered in the affirmative."

In support of his decision, counsel cites sections 800, 801 and 802 of the act approved October 3, 1917.

Stamp Tax on Trade Acceptances

September 13, 1918

(182) The following ruling has been made by the Deputy Commissioner of Internal Revenue as to who should affix the revenue stamps to trade acceptances:

You are advised that the drawer, as the person "who makes, signs, or issues" a trade acceptance, should affix and cancel stamps covering the tax required thereon under subdivision 6, schedule A, act of October 3, 1917.

There is nothing in the law, however, that would prevent the acceptor from affixing the requisite stamps to a trade acceptance and agreeing with the drawer of the draft as to which of the parties would ultimately bear the expense.

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